ISCTE Business School
Instituto Universitário de Lisboa

IMPLEMENTATION OF A SERVICE-DOMINANT LOGIC IN A PORTUGUESE SME WINE SELLER

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- Spine -

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ABSTRACT

The present master thesis is an applied project focused in a SME in the wine market located in the Lisbon area. The company is a traditional family-based wine seller who lacks a strategic vision of the overall customer experience. Service-dominant logic theoretical frameworks guided the work developed in this thesis.

The literature review framed the research to develop the strategic vision, focusing on concepts such as customer experience, resources, sustainable competitive advantages and value offering density.

The macro environment was analysed in terms of the national economical, social and environmental context to better understand the Portuguese wine market.

A consumer analysis allowed the characterization of the wine Portuguese consumer while the internal analysis determined the company's current situation in terms of market development and financial solidity.

The definition of the new strategic paradigm unbundled and rebundled the customer's experience to allow for a comprehensive strategic vision divided into 10 points of contact for the company.

A financial analysis was done to access the viability of the proposed actions, including a sensitivity analysis that concluded the project is financially solid.

The new strategic paradigm gives the company a sustainable competitive advantage for the future.

Keywords: Service-dominant logic, costumer experience, wine SME, strategic marketing

RESUMO

A seguinte tese de mestrado é um projeto aplicado, focado numa PME no mercado dos vinhos localizada na região de Lisboa. A empresa vende vinhos e tem um forte cariz de tradição familiar carecendo, no entanto, de uma visão estratégica que englobe a experiência total do consumidor. Quadros teóricos focados na *service-dominant logic* orientaram o trabalho desenvolvido nesta tese.

A revisão literária enquadrou a pesquisa para desenvolver a visão estratégica, focada em conceitos como a experiência do cliente, recursos, vantagens competitivas sustentáveis e *value offering density*.

O macro contexto foi analisado em termos do enquadramento económico, social e ambiental para compreender melhor o mercado do vinho Português.

Uma análise ao consumidor permitiu a caracterização do consumidor de vinho Português enquanto a análise interna determinou a situação atual da empresa em termos de desenvolvimento de mercado e solidez financeira.

A definição do novo paradigma estratégico desagregou e recombinou a experiência do cliente para permitir uma visão estratégica compreensiva dividida em 10 pontos de contato para a empresa.

Uma análise financeira foi realizada para estudar a viabilidade das ações propostas, incluindo uma análise de sensibilidade que concluiu que o projeto é financeiramente sólido.

O novo paradigma estratégico confere à empresa uma vantagem competitiva sustentável para o futuro.

Palavras-chave: Service-dominant logic, experiência do cliente, PME vínicola, marketing estratégico

ACKNOWLEDGMENTS

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EXECUTIVE SUMMARY

Portugal is currently facing an economical crisis deepened by the austerity from the public spending cuts and tax increases imposed by the three external institutions referred to as *Troika* (ECB, IMF and European Commission) as a consequence for the national bailout. Thus, the purchasing power is decreasing and consumers become more selective in the products they buy. Therefore, companies need to differentiate now more than ever from their competitors to gain the consumer preference.

These effects are naturally present in the wine market where consumers have a wide variety of choices to buy from. This work focuses on a SME in this sector with a traditional family-based top management with limited resources in need to develop a new strategic vision in order to gain sustainable competitive advantages. For confidentiality purposes the company's name is not revealed.

The literature review developed in light of service-dominant logic framework, the Portuguese macro analysis and the company's internal assessment confirms the need for a change in the company's paradigm.

This strategic vision should involve the consumer in the value creation process through the experiencification (Normann, 2001) of wine consumption. The company therefore should shift the paradigm from a wine selling company to a company that sells the experience of wine consumption. This will allow the creation of a denser value offering for the consumer.

The final outcome is the unbundling of the consumer's experience into 10 stages: Occasion, Intention, Information, Informed decision, Channel, Purchase, Transportation, Conservation/Offering, Consumption and Waste. The works shows how the company can, in each stage, add value to the customer and integrate him/her in the value creation process while at the same time incentivizing the next order. Hence, the company's strategy translates into a comprehensive value added process of the consumer's wine consumption experience. No single proposed action is sufficient by itself to differentiate the company in the market but it is rather the sum of the actions and their integration in the overall experience that may result into a sustainable competitive advantage. To build it and consolidate it is required to develop a long-term tangible or intangible asset, valued by costumers, which competitors don't possess. The implementation of such strategy requires the company's top management to be fully committed to its success as it represents a fundamental change in the company's *modus operandi*.

The financial analysis of the proposed actions concluded the strategy creates economic value and that its top management should implement it. The analysis was done through cost and revenue estimative based on reliable external and internal sources. To further asses the financial robustness of the projections, a sensitivity analysis based on variations of the implied interest rate and their impact in key results was conducted. This sensitivity analysis backed the previous results and allowed to conclude the validity of the strategic recommendations.

The proposed strategic vision shifts the company's paradigm, giving it a sustainable competitive advantage with the objective to gain the consumers' preferences in order to face the ever more challenging market, through a series of financially viable set of actions.

IDENTIFICATION OF THE TYPE OF THESIS

The thesis is an applied project. It will identify and develop an integrated framework to a new service dominant logic for an existing company, supported by a thoroughly review of the company main characteristics and by the use of key concepts and frameworks driven by the literature review. The quest is for a fundamental understanding of relevant issues and how to cope with them linking theory and relevant practice.

Theme

The object in which the analysis of the thesis will focus on is a wine company located in the Lisbon region. For confidentiality reasons the company will never be identified and it will always be referred to as “the company”. The company is a family business, dating from the 60’s decade, with over 40 years in the wine selling business. The company has a wide variety of products, from the cheapest to the upper wines. The cheapest wines have always represented the larger share of revenues. Due to the traditional familiar context, the company lacks a true strategic and marketing oriented strategy, with no real long-term commitments. Decision-making processes have been based on previous experiences, rather than data-oriented decisions. Theoretical frameworks and data collecting methods will be used to redesign this SME, in to an innovative company. The focus will be to prepare the implementation of a service dominant logic.

Research Problem

The challenge proposed will be “How can a Service Dominant Logic be implemented in a Portuguese SME dedicated to sell wine products and what are the consequences of such implementation?” The research will reflect the shift this service oriented approach c requires and how it can be accomplished in such a company. Theoretical frameworks will provide the basis for the analysis and the conclusion drawn from it.

Objectives

The objective of such a thesis is to provide strategic view based on scientific frameworks and allow the implementation of data-oriented decision making processes. In detail:

- Explanation of key theoretical concepts and main frameworks to be used
- Analyse the company’s current situation,
- Determine the company’s main problems and constraints

- Establish a strategic view and business concept based on previous inputs and frame it in terms of the appropriate theories

LITERATURE REVIEW

According to the European Union, "an enterprise is considered to be any entity engaged in an economic activity, irrespective of its legal form. This includes, in particular, self-employed persons and family businesses engaged in craft or other activities, and partnerships or associations regularly engaged in an economic activity" (Commission recommendation, 2003). Within this wide range of enterprises there are the small and medium enterprises (SME). However, the definition of Small and Medium Enterprises is not a clear and unique one around the world. In Europe the SME are defined as (Commission recommendation, 2003):

"1. The category of micro, small and medium-sized enterprises (SMEs) is made up of enterprises which employ fewer than 250 persons and which have an annual turnover not exceeding EUR 50 million, and/or an annual balance sheet total not exceeding EUR 43 million.

2. Within the SME category, a small enterprise is defined as an enterprise which employs fewer than 50 persons and whose annual turnover and/or annual balance sheet total does not exceed EUR 10 million.

3. Within the SME category, a microenterprise is defined as an enterprise which employs fewer than 10 persons and whose annual turnover and/or annual balance sheet total does not exceed EUR 2 million."

Being a SME, in the European Union may be beneficial mainly in two perspectives:

- Fewer requirements or reduced fees for EU administrative compliance,
- Eligible for funding supports, under EU-business support programs specifically for such companies.

Company category	**Employees**	**Turnover**	Or **Balance sheet total**
Medium-sized	< 250	≤ € 50M	≤ € 43M
Small	< 50	≤ € 10M	≤ € 10M
Micro	< 10	≤ € 2M	≤ € 2M

Table 1 – EU Definition of Enterprises size

The importance of strategic planning in large corporations has been the subject of an extensive array of research. In SME's however, there is a current debate on whether SMEs need a competitive strategy that guides investment and market behaviour by defining constraints or whether their competitive advantage stems from their ability to respond flexibly to market needs, particularly in today's highly competitive environments where continued adherence to a specific strategy can even harm competitiveness (Leiter. 2009; Hair et al. 1998; Zhara et al. 2008). Some argue operational efficiency and tactic is enough for SMEs to gain an advantage in the market (Zhara et al. 1993). Other, that it's the commitment to a certain strategy over a period of time that allows for sustained competitive advantage (Leitner, 2009).

Sustained competitive advantage has been a concern in the resource-based view. According to Barney (Barney, 1991) the firm's resources must possess certain characteristics, in order to able to create sustainable competitive advantage. Barney defines firms resources as "all assets, capabilities, organizational processes, firm attributes, information, knowledge, etc. controlled by a firm that enable the firm to conceive and implement strategies that improve its efficiency and effectiveness". These resources can be summarized as the company's strengths. A competitive advantage is a value creating strategy that competitors are not implementing (Barney, 1991). A sustainable competitive advantage is a value creating strategy that gains superiority over the competitors, through a long period of time (Barney, 1991). The sources of sustained competitive advantage derive from two factors. In order to create such strategies the firms must possess different resources (resource heterogeneity) and cannot move from one firm to another (resource immobility). If all companies pose the same resources, homogeneous resources, no one is able to adopt a value creating strategy without the others implementing that same strategy (Lieberman & Montgomery, 1988). However, even if resources are homogeneous, entry barriers may allow for firms to gain sustained competitive advantage, compared to companies which are not within the industry (Barney, 1991). The higher the resource immobility, the easier it is to gain sustainable competitive advantages. Sustained competitive advantage comes from resources with all of the below characteristics (Barney, 1991):

- **Value** – resources must be able to create value. Resources create value if they allow for gains in effectiveness or efficiency.
- **Rareness** – if resources are to allow for sustained competitive advantage, not all firms may have the resource. Otherwise the value creating strategy could be

adopted by a variety of firms, giving no one an advantage regarding its competitors.

– **Imperfect Imitability** – companies can be first-movers with valuable and rare resources. However, the strategy is not sustainable, meaning it concedes an advantage during a large period of time, if competitors are able to quickly imitate the rare resource. If the resource can be copied, firms will copy it and eliminate the advantage. This imperfect imitability can be due to historical reasons – the capacity to exploit a certain resource may have a time and place constraint; causal ambiguity – if it is not clear what is the cause and effect process competitors are not able to understand it and copied it; or social complexity – the ability to exploit a certain resource may be intrinsically connected to a complex social reality, and such other companies cannot replicated elsewhere.

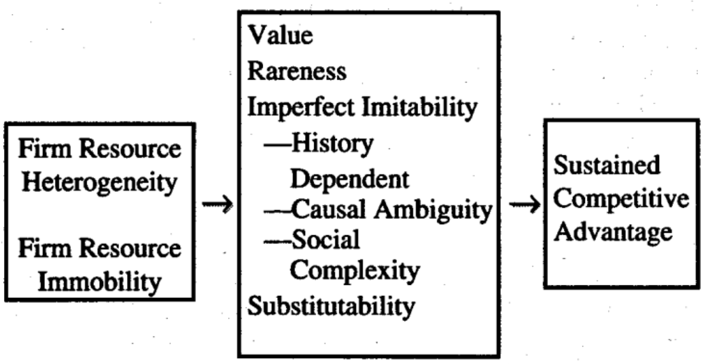


Figure 1 - Barney's framework; Relationship between sources, characteristics and outcome

The framework in figure 1 (Barney, 1991) explains the relation between the sources of resources that allow for sustained competitive advantages, its characteristics and the final outcome.

However, even with the right resources, with all of the characteristics, the firm must be able to have the capabilities to take advantage of such resources. Creative business thinking is thus required in order to create innovative strategies. Normann argues that companies need to adopt a service-dominant (S-D) logic to become first-movers (Normann, 2001). Lieberman and Montgomery (Lieberman & Montgomery, 1998) define first-mover advantages as the pioneer's ability to earn profit. The evolution of strategic paradigms, in order to create sustained competitive advantages, has moved from a production orientation to a relationship orientation to a new archetype of organizations—the business company as an organizer of value creation (Normann, 2001). With this new orientation comes the shift from a firm-centric to a customer-centric perspective. The role of the customer changes from a receiver of goods and services, to being a participant in the value creation process. Normann advocates companies need to analyze the value constellation, as oppose to the value chain of the business. This value constellation deals with of the participants in the business-making process, its stakeholders, and analysis where value can be created. In a review of Normann's book the authors stated "this co-production, or co-creation of value, function is not a special case limited to services, as traditional goods-dominant (G-D) logic and the related neo-classical economic model would suggest, but rather the fundamental joint role of the firm and the customer in value creation" (Michel, 2007). This integration of the different stakeholders, in a joint co-productive value creation gives a more dilated view of offerings, which according to Normann transforms offerings into "artefacts designed to more effectively enable and organize value co-production".

This involves reframing the firm's business, through a process of upframing, meaning "consideration of the overall system of which the firm is a part" (Michel, 2007), preventing company "myopia" (Levitt, 1960).

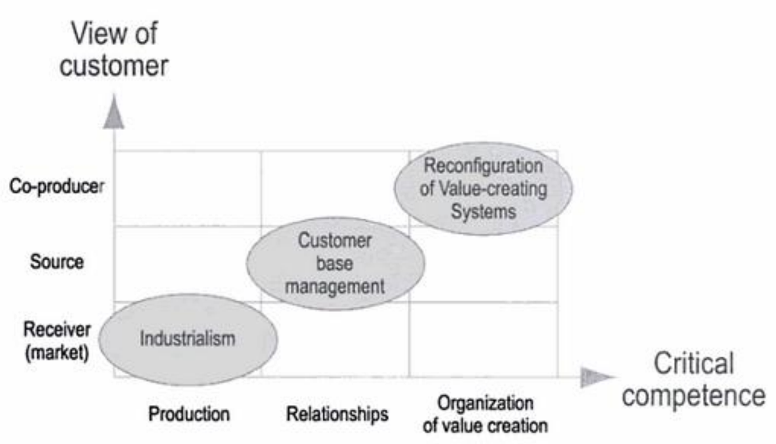


Figure 2 - The evolution of strategic paradigms, Normann 2001

From a historical point of view, Normann states companies should move from a customer base management to a reconfiguration of value-creating systems. In past companies were able to move from an industrialism perspective to the customer base management by changing its core competence and the way the customer is viewed. The critical competence, meaning the capability the firm exceeds in performance, should evolve from managing relationships with customers to organizing the value creation in the value constellation (Normann, 2001). Also, the firm should view the costumer not as a source of business, in an outflow process from the customer to company, but rather as a co-producer of value. IKEA, for instance was able to pass the assembly process, a value creating process, to the consumer, making the available

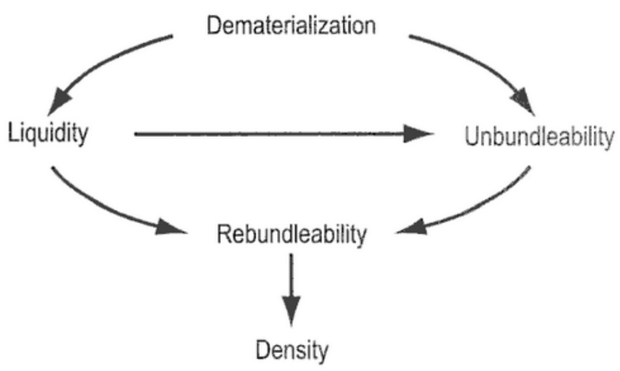


Figure 3 - Drivers promoting density (Normann,2001)

space in the customers' living room usable, rather the stores' own space (Normann, 2001). This reconfiguration, or reframing process, leads the way to innovation. "Innovation, within the context of value constellations and customer communities, is less likely to occur linearly through value chains but rather it emerges dynamically from newly created value constellations" (Michel, 2007). These value constellations "identify economic actors and link them together in new patterns which allow the creation of new business that did not exist previously, or (...) change the way certain types of value are created. This is not about a simple reallocation of existing activities between a set of actors, but of constructing a new, coordinated set of activities resulting in a new kind of output" (Normann, 2001).These re-definers of systems of value creation are called Prime Movers (Normman, 2001).

Another concept emerging from the service-dominant logic of Normman and others is the concept of density of offerings. Density refers to "the best combination of resources [that] is mobilized for a particular situation—e.g. for a customer at a given time in a given place—independent of location, to create the optimal value/cost result, and the term itself expresses the degree to which such mobilization of resources for a 'time/space/actor' unit can take place" (Michel, 2007; Normman, 2001). In order to create new density Normann describes two processes - liquification and unbundleability (Michel, 2007). According to Normann, "liquification refers to dematerialization through the separation of information from the physical world, allowing it to be easily moved about" (Normann, 2001). "Unbundleability refers to the separation of "activities hitherto well defined and held together in time and place and by an actor" (Normann, 2001) much like what IKEA done with the assembly of furniture, whose process was moved forward along the all experience of buying furniture (IKEA was able to have customer buying the piece first and only assembly them later). "This dematerialization through liquification and unbundleability promotes rebundleability, which allows the creation of new densities capable of being combined with customer resources to create new value configurations", thus allowing for companies to become prime-movers (not to be mistaken with first-movers) by reconfiguring the value creating process.

Normann describes 3 trends in offerings that still hold relevant for today's marketplace:

- ***Servicification*** - the offers have shifted the focus from the product to the use of the product.
- ***E-fication*** - some parts can be performed in the dematerialized information domains while other parts still have to be performed in the domain of physical activities.
- ***Experiencification*** - Is about creating a connection with between the client and the product; the mental and symbolic processes of the customer. It is possible to interactively rebundle what has been unbundle into new patterns, which create value creating offers, with the highest density possible. The information is now largely free to the consumer, so we must find new price carriers and create new business models.

The following table summarizes the shift in concepts the Service-Dominant logic requires for creative business thinking (Normann, 2001).

Goods-Dominant Logic	**Transitional concepts**	**Service-Dominant Logic concepts**
Goods	Services	Service
Products	Offerings	Experiences
Feature/attribute	Benefit	Solution
Value-added	Co-production	Co-creation of value
Profit maximisation	Financial engineering	Financial feedback/learning
Price	Value delivery	Value proposition
Equilibrium systems	Dynamic systems	Complex adaptive systems
Supply chain	Value-chain	Value-creation network/constellation
Promotion	Integrated marketing communications	Dialogue
To market	Market to	Market with
Product orientation	Market orientation	Service orientation

Source: Lush and Vargo (2006, p.286)

Table 2 - Conceptual transitions from a Goods-Dominant Logic to a Service-Dominant one

Richard Normann, (Normann, 2001) designed a framework, to help business reconfiguring the value creating system, which he named “The Crane Model”. This tool deals with different time frames and conceptual system thinking.

1. **Taking stock: What are we?**

This process deals with going back to the company’s history to find values and purpose of the organisation and structural arrangement. It is interesting to find successes and failures. The idea is to find and identify possible “hubs of reframing” (assets, capabilities, customer relationships and customer bases).

2. **Up framing of business systems**

Unfortunately this step often stops as a simplistic or even linguistic exercise of no commitment and no consequence. For the ones that really rethink, the consequences may be dramatic and beneficial. IKEA and Coca-Cola, for example, transformed themselves based on a grounded, thoroughly reflected, and visionary up framing concept (Normann, 2001). The result was more than creative marketing. Up framing means redefining the boundaries of the system we are in at the moment. It is important to stimulate the creativity but it essential to be solid, relevant throughout the whole process so that the up framing is grounded, legitimate and actionable. There are some steps to follow:

- Studies of invaders
- Value stars of the organisations' customers (as well as the customers' customers). This means analyzing their business, how they contribute to their customers and how their invaders are competing.
- Design several blueprints for alternative co-productive value constellations.

3. Travelling in conceptual time: Time framing

Up framing is a good start where several hypotheses are created. Value creating systems and a focus on the organization's role could be helpful. The next step is to increase the conceptual design space – and move into the future. There are two ways of creating scenarios and they may as well be complementary. The first one is the *conceptual scenario.* The other is to create scenarios in the *opportunity space*, which will be described below. Conceptual scenarios identify the key driving forces and the pros and con for the scenario- everything that might affect the company's activities.

4. Creating strategies scenarios in the opportunity space

Organizations can make choices. Normann prefers to be more direct and focused on the business of the organisation. It is useful to focus more in the specific role in this redefined "value creating system" of the focal organisation. If the result of the up framing and the time framing processes is the unfolding of an opportunity space, perhaps some first strategy scenarios need to be made more robust and testable. Two or more such alternative designs should be brought to surface.

5. Back to here and now: Translating a vision into a business idea

These processes require some iteration but if the up framing and artefact scenario making (time framing) has been successful, the managers have received a wide variety of creative ideas. However, one cannot yet talk about new business or action plans. The vision of the chosen strategy could be tested for solidity against different conceptual scenarios. A business idea should be blueprinted and then tested.

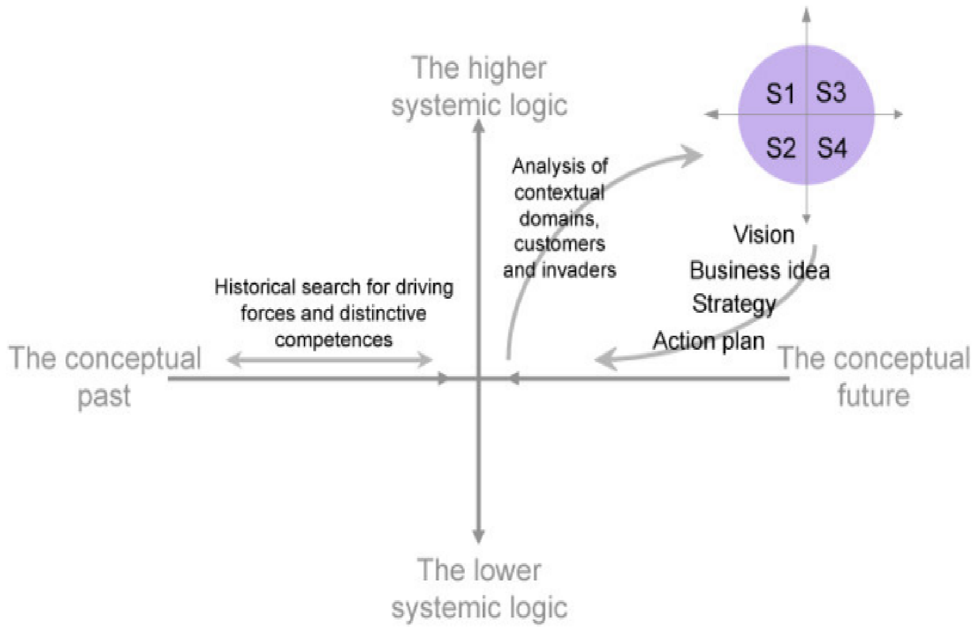


Figure 4 - The Crane Model

The final objective is to have a strategy that is adequate to the company and allows for innovative business thinking, changing the landscape in which the company will operate, by re-organizing the value creation process.

CONTEXT

Economical context

Portugal is currently under a financial aid from the so called “troika” (a tri-party committee composed by the IMF, the ECB and the EC). The rescue was considered to be a necessary measure as Portugal was paying an unsustainable level of interest rates on its public debt. Associated with the financial rescue , worth €78b (of which 12b were destined to the financial sector, to help in the recapitalization process) that started in April 2011, was an economical re-structuring plan oriented to reduce the government’s deficit and public debt through a series of reduce public spending and tax increases. As such, the proposed recessive measures had its effects in the real economy affecting negatively both the level of investment and consumption, and consequently, its GDP growth.

Gross Domestic Product (billion euros)

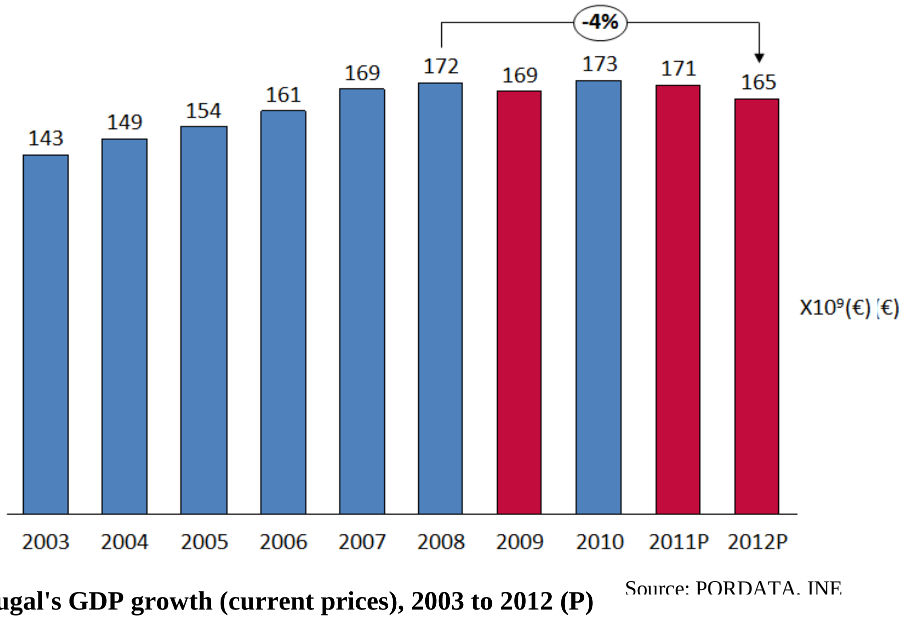
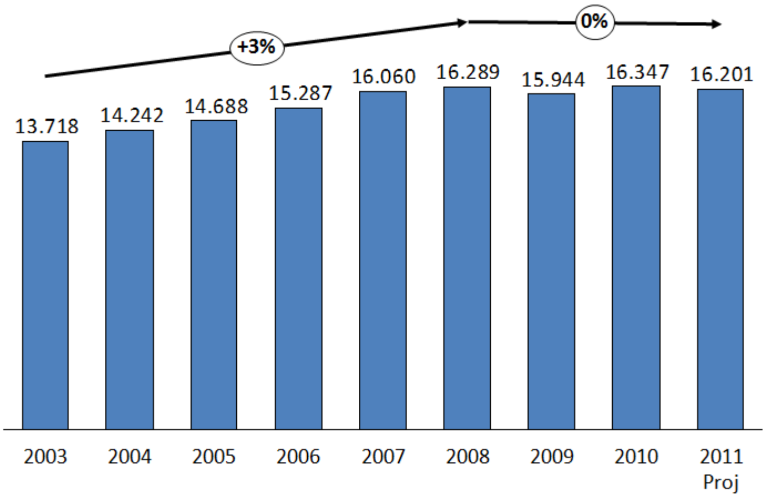


Figure 5 - Portugal's GDP growth (current prices), 2003 to 2012 (P)

Portugal had experienced a GDP growth up until 2008, the same year when Lehman Brother went bankrupt and the global financial crisis began, reaching an approximate value of €172 billion. 2009 was the first year of the current recession, with a significant decrease, of approximately 1,7%. Although in 2010 there was a slight recovery, in 2011 and 2012 economy plunged again. . The decrease in GDP reflects the decrease in public and private consumption and investment. The State, conditioned by the financial aid rescue plan and lack of funding, decreased its public investment levels. The recessive measures undertaken, especially the increase in tax levels, have cut the consumer’s purchasing power, reducing consumption. Facing a lower consumer spending and also scarcity in the credit from banks, who have been in an accelerated deleveraging process to regain financial slack, , companies in the majority of the cases highly dependent of the internal market, have also reduced its level of activity.

GDP per capita (€) and CAGR



Source: PORDATA, INE

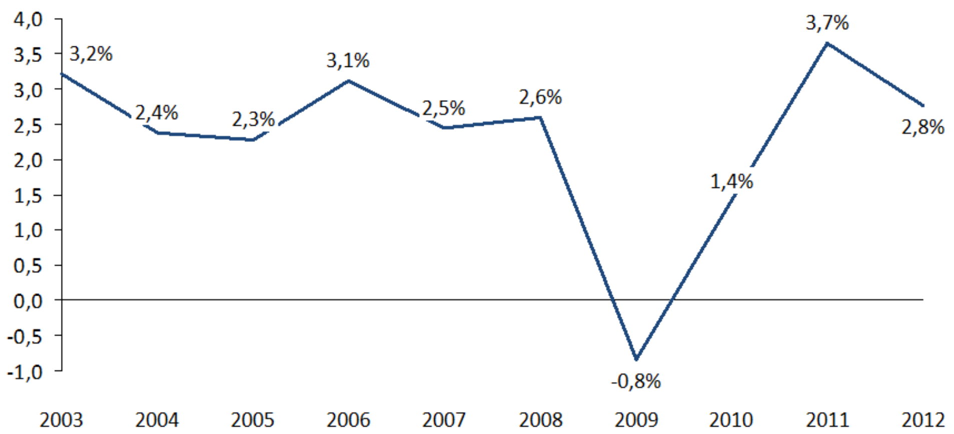
Figure 6 – Portugal's GDP per capita (€) and CAGR, 2003 to 2011

In terms of purchasing power, the GDP per capita provides a useful insight as it accounts for the total GDP divided by the size of the population. Several factors can influence the growth/decline of GDP. By taking into account the population factor, GDP per capita provides a more accurate measurement to access a country's wealth. The per capita value can be interpreted as an approximation of the average income each inhabitant disposes to consume, save or invest[1]. As the figure shows, there has been 2 moments in the last decade. From 2003 until 2008, GDP per capita had a compound annual growth rate (CAGR) of 3%. However, since 2008 until 2011 (2011 with projected values) the CAGR was 0%. In this last 4 years GDP per capita has had an irregular behaviour, growing only in 2010 and decreasing in 2009 and 2011. This decrease in GDP per capita reflects the decrease in the consumer's purchasing power, which in turn will be reflected in the economy's total spending. The problem with a stagnated GDP per capita, other than the fact it being synonymous of a stagnated or recessive economy, is the decline in real purchasing power. Up until now the indictors have been analyzed considering the current prices methodology, meaning the inflation impact was included. With a stagnated purchasing power and a positive inflation,

[1] Inequalities in wages distribution distort this approximation, as a small group of individuals may concentrate a high amount of the total national income.

consumers are in fact reducing their purchasing power. If the income is the same but prices are higher, the same income is not able to buy as many products/services as before and consumers are actually worse than they were.

Inflation (CPI)



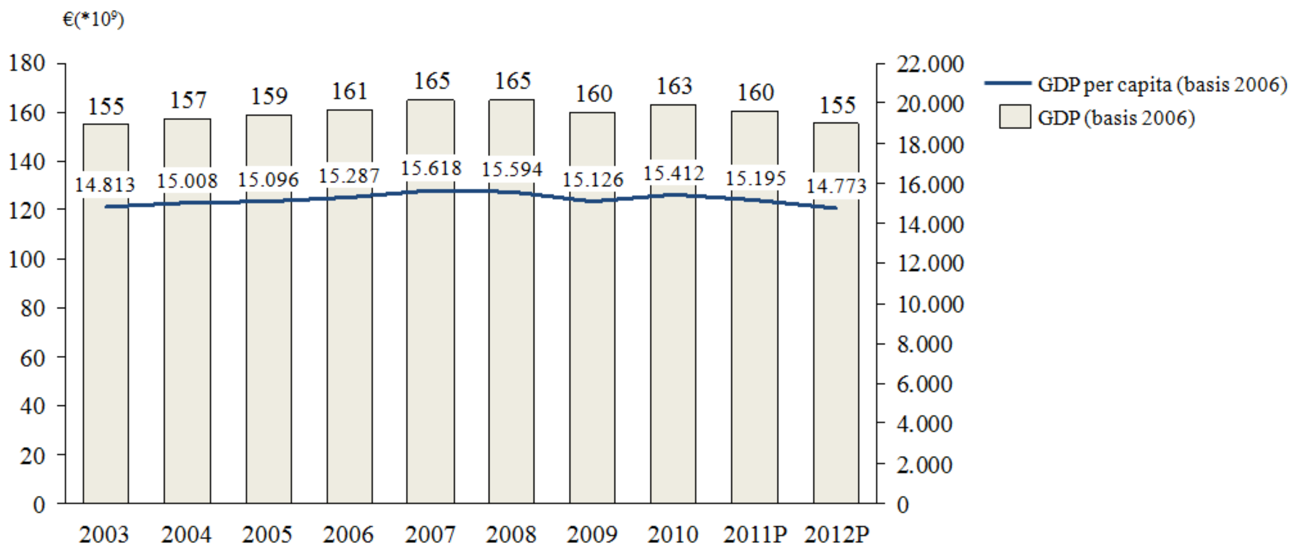
Source: PORDATA, INE

Figure 7 – Portugal's Inflation (CPI), 2003 to 2012

Inflation has been positive in the last decade, for a single exception in 2009 with a 0,8% decrease in the general level of prices, designated as deflation. The negative impact of inflation is it can create a "false" growth. Since GDP at current prices is calculated as the sum of private consumption, public spending, total investment and the net effect of the balance trade, higher prices will result in higher absolute values from the total Gross Domestic Product.

Therefore it becomes necessary to analyze the real increase both in GDP and GDP per capita to assess how the Portuguese economy as evolved, without taking into consideration the effect of inflation.

GDP and GDP per capita at constant prices



Source: PORDATA, INE

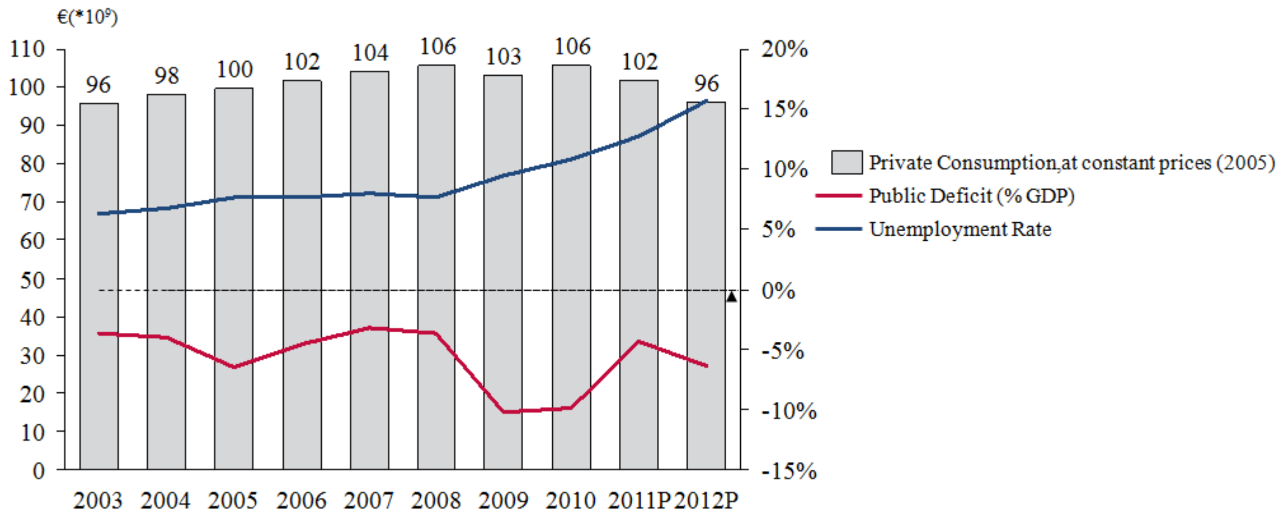
Figure 8 - GDP and GDP per capita (basis=2006), from 2003 to 2012

Analyzing the values at constant prices, it is possible to see that the last ten years were a "lost decade" as the GDP and GDP per capita values for 2012 are the same as in 2003.. Portugal in the last ten years was not able to generate real growth, lagging behind its European counterparts.

The economic downturn has several social impacts. If the economy is not growing, then people aren't gaining purchasing power, families aren't consuming more which in turn means companies aren't selling more, and thus they don't invest as much and don't increase their workers' wages nor create additional jobs.. Companies that can't resist the crisis and are going bankrupt mean more people are left without a job. For State this as 3 main negative consequences. The first one is it can't collect as many direct taxes, either from families or companies, through their income. The second one is that it has to pay more unemployment benefits, which naturally increases public spending. Finally, the third one has to do with the indirect taxes. If consumption is decreasing then the amount of VAT collected also decreases[2].

[2] According to the PORDATA website, in 2012, VAT revenues account for nearly 40% of total taxes revenues

Portugal's Key Economic Indicators



Source: PORDATA, INE

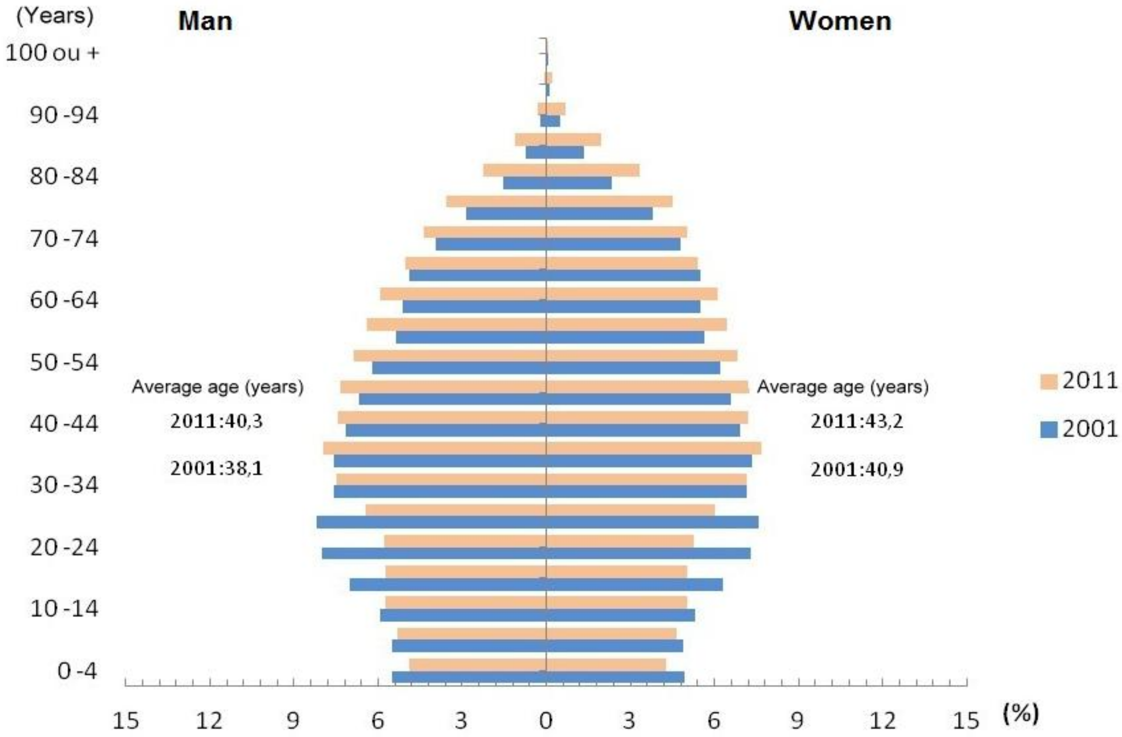
Figure 9 – Private Consumption at constant prices, Public Deficit (% of GDP) and Unemployment Rate

Figure 9 somewhat summarizes the Portuguese economy in the last 10 years. With a constant public deficit, meaning there's a need for the State to increase taxes or cut down spending now or in the future, the unemployment rate has had a nearly-constant upward movement. In fact, from 2003 until 2012 the unemployment rate has risen nearly 150%, from 6,3% (2003) to 15,7% (2012). However, there are two trends concerning the unemployment rate. Although both reveal an upward trend, from 2003 until 2008 the unemployment rate has risen at a slower pace, from 6,3% (2003) to 7,6% (2008). However, in 2009, there is sharp increase and the unemployment rate moves from a value of 9,5% (2009) to 15,7% (2012). So, while in the first six years the unemployment rate has risen 21%, in the last four years it has risen 65%. Private consumption, presented here at constant prices (without the distortion of inflation), has had a more erratic behaviour. It has had a steady growth from 2003 until 2008, rising 10% for the 6 years period. However, the start of financial crisis in late 2008, cause people to be more cautious in their spending which resulted in decrease in 2009 of approximately €3b in private spending. In 2010, people resumed their 2008-level of spending of nearly €106b but as unemployment continue to grow and government raised the tax level to face the public deficit and to accommodate the troika conditions, the consequences were felt in 2011 and 2012 with a decrease in private consumption of 4% and 6%, respectively. It's important to highlight that, much like the GDP and GDP per capita (both at constant prices [2006]), the private consumption in 2012 is equal to the 2003 levels.

The current economic context is not a prosperous one for companies and families. More and people experience what it is to unemployed which naturally has a severe impact in their spending patterns, cutting down in their overall consumption budget. For companies this means a decrease in the total market value and number of consumers. This decrease in market size result in a more competitive environment for companies to deal with, as each one strives to gain more market share in a decreasing market. The increased competition in the overall market, make it so much essential for companies to be more flexible, more innovative and to gained what was defined previously as a sustainable competitive advantage. In fact, the crisis and consequently increased competition , has given consumers more bargaining power because it made it so much essential for companies not to lose current customers and that much difficult to gain new ones. The wine market, as expected, was also hit by this adverse economic environment. Wine companies also need to be more agile and adapt to this during/post crisis market. Companies that are able to adapt and understand the “new” and more demanding customer will be the ones to succeed in the future. Thus, it becomes imperative, now more than ever, to have a clear and well defined strategy and change the mindset from selling products to selling experiences, as seen in table 2.

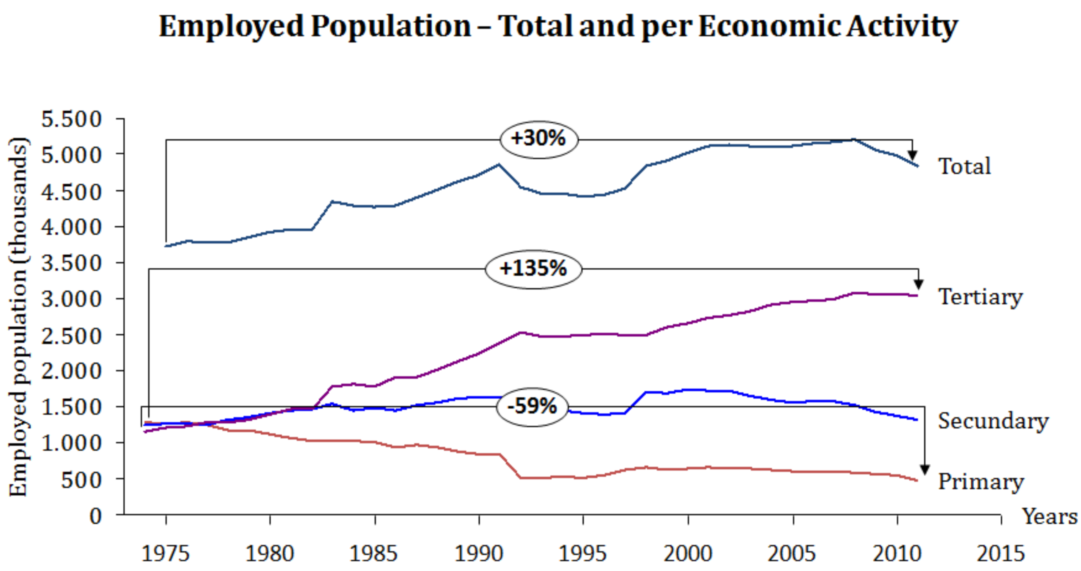
Social context

According to the 2011 Census, Portugal has a population of 10,6 million, where 48% are men and 52% are women (5 046 600 and 5 515 578 individuals, respectively). The same source indicates 84% of the population lives in Lisbon or to the north of it, in the North or Centre, according to the NUTS II designation (27% lives in Lisbon, 35% in the North, and 22% in the South). Alentejo has 7,2% of the total population, Algarve 4,3% and the islands only 4,8%. Thus, the population is unevenly distributed, with the great majority of the population between the North and Lisbon, especially near the ocean where most cities are located. In terms of age distribution (as showed in the graph below) Portugal is an ageing country. In ten years, from 2001 to 2011, the population's average age has increased roughly 2 years. People between 25-64 years represent 55,2% of the population. However, people 65+ years already represent 19% of the total population, when compared to 16,4% in 2001.



Source: INE, 2011 Census

Figure 10 – Portugal's age distribution, by gender, in 2001 and 2011



Souce: PORDATA; INE

Figure 11 – Employed Population – Total and per Economic Activity

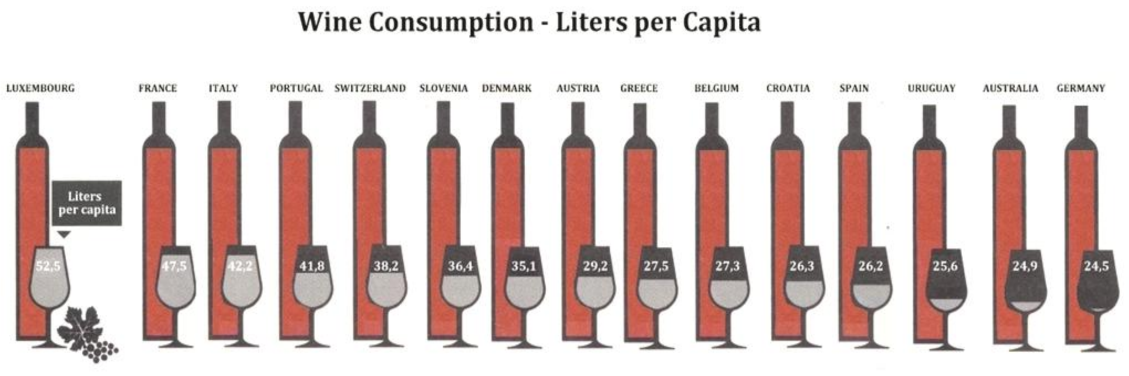
In terms of workforce allocation, the primary sector has been losing workers. Although it used to be where most of the population worked, in the last decades it has been losing terrain to the tertiary sector. In a matter of 37 years the population employed in the primary sector has decreased 59% while the tertiary sector has gained 135% more workers. However, it must be said that the advance in agriculture techniques has increased productivity, allowing for workforce to be reduced while keeping the level of production. Also, with the professionalization of many small private farmers, and increased regulations and obligations to fulfil, a small percentage of the tertiary sector is in fact working for the primary sector as service providers. Accountants, lawyers or finance managers are such examples. Nonetheless, even considering those factors, there has been an exodus, especially of young people, that prefer to abandon the uncertainty and hard working jobs of agriculture to move to urban areas in pursuit of better living conditions.

The History of Wine in the Portuguese Society

Wine has been cultivated in Portugal ever since before Portugal was even a country. Its history is closely related to the wine history as it's a part of the Portuguese culture. It is believed the first vineyard planted in the Iberian Peninsula was in 2000 BC, in the Tejo valley and the Sado valley by the Tartessians, who lived in what is now called Andalusia, Spain (Phillips, 2000). The Phoenicians introduced new grape varieties and took over the Tartessians wine trade around the X century BC. Up to this point in history, viticulture was done mainly around the southern coastal areas of Portugal. When the Greeks settled in the Iberian Peninsula in the VII century BC they contributed greatly to the viniculture development and brought new techniques with them. In Alcácer do Sal, an archaeological discovery found a cratera, a vase used by the Ancient Greeks to drink wine, proving Ancient Greeks drank Portuguese wines. The Celts in the VI century BC introduced new wine varieties in the Iberian Peninsula but it was with the Roman's ruling that the vineyard culture and trade truly developed. Only when part of Portugal was under Arab rule did the wine production in the region decreased. The cause was the Arab religious beliefs, which forbid alcohol consumption. However, during the Reconquistas in the XII and XIII centuries AC, the wine production began to once again become a priority. During this period, some new varieties were added to the ancient ones, for instance Frenchs varieties such as Burgundy. Henry, count of Portugal and father of D. Afonso Henriques, Portugal's first king, was from the Burgundy region so there's no surprise this variety made its way to Portugal.

With the country's independence in 1143 (the recognition of the Holy Se), wine became the most exported product. England was where Portugal exported the most. This was due to historical reasons, for instance with the signing of the Treaty of Windsor in 1386 (Portuguese National Archives Digital Collection), today's oldest diplomatic alliance, or the Methuen Treaty in 1703, which stated that no taxes with be charged on Portuguese wines. It was around this time that the famous Port wine gained popularity in England and, in 1756, the Marquis of Pombal established the world's first "protected designation of origin" (PDO or DOC in Portuguese) for the production of authentic Port from the Douro region (Robinson, 2006).

Today, wine continues to have a major relevance in the Portuguese culture. In fact, Portugal is the 4th country in the world in terms of wine consumption per capita (see graph below).

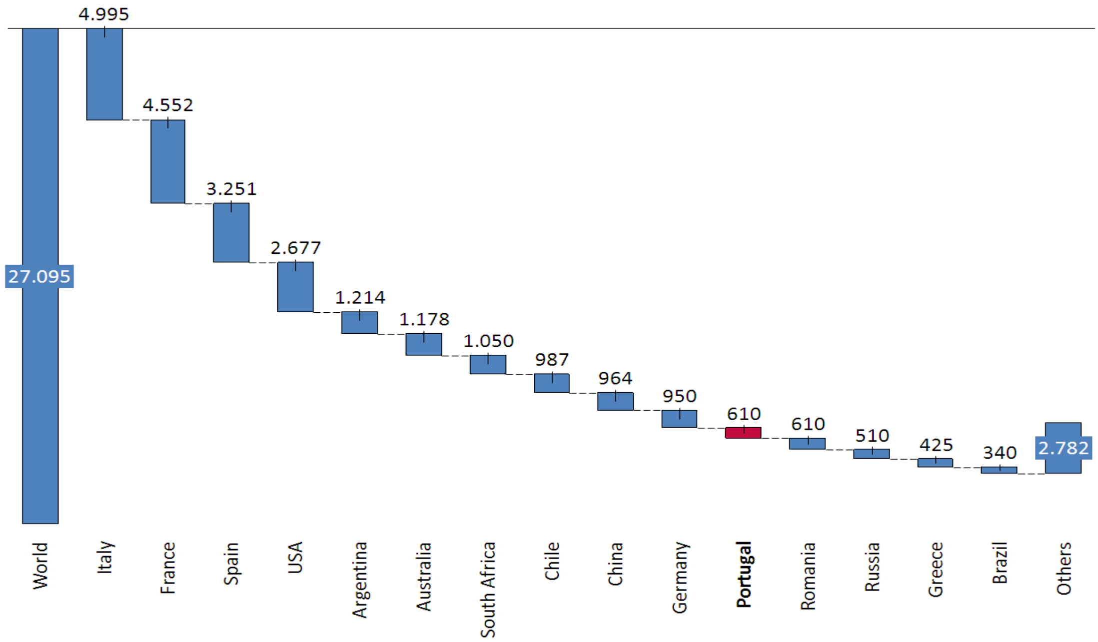


Souce: The Wine Institute, 2010

Figure 12 – Wine Consumption – Liters per Capita

In fact, besides Luxembourg, Europe and particularly Southern Europe (France, Italy and Portugal) occupies the leading positions when it comes to wine consumption per capita. Historical and social reasons account for this high per capita levels in those countries. France and Italy, much like Portugal, have their vineyards tied to their countries' History.

Top 15 countries in wine production, per million liters in 2009



Source: University of Adelaide, Global Wine Markets, 1961 to 2009: A Statistical Compendium

Figure 13 – Wine production per Country, Millions of Liters, 2009

In terms of litters production however, Portugal falls to the 11th place in the world. On the one hand, Portugal is a small country and thus limited by its geographical limits. On the other hand it has the world's highest percentage of cropland under vines (13,47%) against Italy's 8% or France's 4,23%, according to the University of Adelaide, Australia.

Portugal is undoubtedly a wine consuming country. Wine has been a part of Portugal's history and drinking it is something that is embedded in the country's traditions and collective identity. This represents both an opportunity and a challenge. On one hand there's an opportunity to sell wine as the country is somewhat of a "natural consumer" and drinks wine in celebrations, family meetings, everyday meals and all kinds of moments. On the other hand there is the challenge for companies to stand out from competitors, in a market that has literally hundreds of years.

Environmental Context

According to the European Union “Wine shall be the product obtained exclusively from the total or partial alcoholic fermentation of fresh grapes, whether or not crushed, or of grape must”[3]. Therefore the environment plays a crucial role in the wine production and consequently in its quality. It’s necessary to understand the environmental context to fully identify the opportunities and/or threats surrounding the wine market in general.

The vine is a woody perennial plant that will only produce grapes 3 or 4 years after it has been planted and has a lifespan of 30 to 50 years. Like any other plant it has its own cycles during the year, depending on the seasons:

- In late Autumn and throughout the all Winter, the vine stays in rest, with no leafs of fruits to show
- In the end of winter, if the vine had been pruned during the winter, the start of this cycle is signalled by a "bleeding" of the vine. “This bleeding occurs when the soil begins to warm and osmotic forces pushes water, containing a low concentration of organic acids, hormones, minerals and sugars, up from the root system of the vine and it is expelled from the cuts (or "wounds") left over from pruning the vine. During this period a single vine can "bleed" up to 5 litres of water” (Robinson, 2006).
- In late spring, when the temperature is between 15-20ºC, the flowering begins followed by the pollination and fertilization with the final outcome being a grape berry.
- In the middle of the summer the “fruit set” phase occurs. The grape berry begins to grow in volume and changes colour from green to blue/black or yellow, depending if it a red wine grape or white wine grape, respectively.
- The ripeness phase is a crucial step regarding the wine quality because in this phase the grape berry starts to concentrate sugar and losses acidity and gains aroma. The end of this stage is the harvesting that occurs usually in September/October. After the harvest the cycle re-starts as the days become cooler and the plant’s activity decreases.

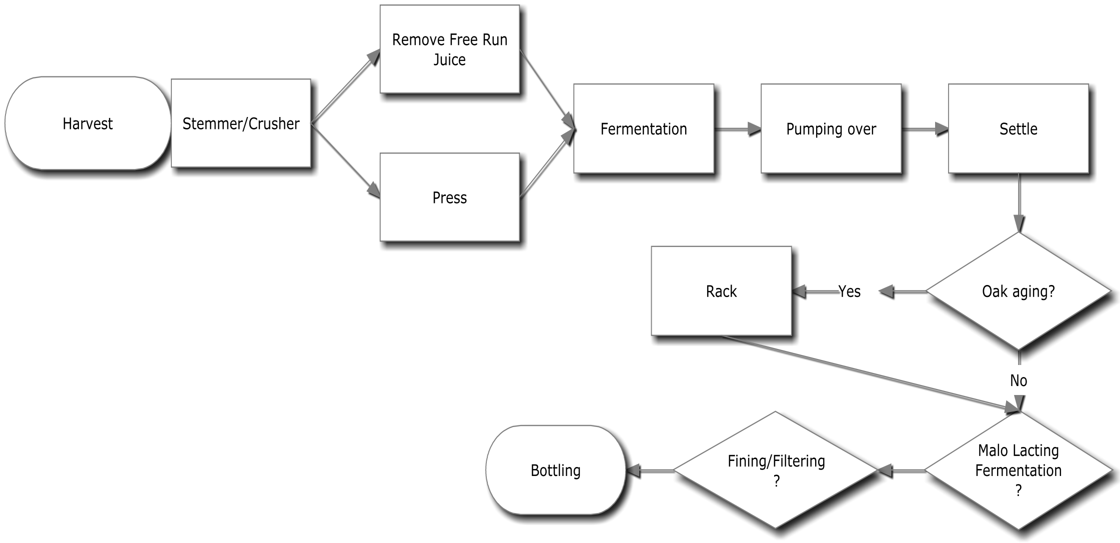
After the harvest, the wine production begins. The grape berry itself has 3 main components: the skin, the pips and the flesh. It is the alcoholic fermentation of the juice of the flesh that originates the wine. Depending on what kind of wine the producer desires, the contact

[3] Council Regulation (EC) No 491/2009 of 25 May 2009

between the solid (skin and pips) and liquid elements (the juice from the flesh) are avoided, reduced or prolonged. Obviously, the variety of the grape berry used to produce the wine will have a key impact in the final outcome.

The wine can either be mono-varietal, if there is only a type of berry used, or multi-varietal if more than one type is used. The decision to blend, or not, different varieties relates to many different factors that the producer may want to achieve. A balance in taste, a desired aroma or longer lasting wines, are some of the reasons to blend different varieties. In Portugal, according to DECO's (Consumer Protection Association) "Guia de Vinhos Proteste", there are 341 varieties of grape berries. According to the same publication, there are five main factors that influence the final outcome of the wine:

- **Variety of grape berries** ("castas") – Each variety has its own flavour proprieties. The blending, or not, of these varieties, will impact the final tasting proprieties. However, wine from the same variety does necessarily have the same taste. Other factors come into play.
- **Soil** – Relatively low fertile, water permeable and heat retaining soils produce the best results. Also, vines need to develop long roots to reach water and minerals, which will protect them against natural adversities.
- **Weather** – Grapes need a certain amount of sun hours to reach full ripening. Also, the colder the weather the less sugar the wine will have, making it more acid. Some other less predictable events also determine the wine quality. Mild frosty soils in the winter, rainy springs and not excessively summers will help to obtain a better outcome.
- **Vine disposal** – the way the vineyard is display, the density of the plantation or the type of pruning used will affect the plants performance and consequently the wine.
- **Wine production process** – the way the process is managed between the harvest until the first sip of the bottle affects the quality of the wine. The more thorough and detailed oriented the process is, the better the final outcome. Quality inspections, transportation conditions, fermentation time, the storage and other steps in the process will influence positively or negatively the quality of the wine. The following figure summarizes the wine production process.



Source: Guia de vinhos Proteste 2010

Figure 14 – The wine production process

The environment plays a key role in the quality of the wine produced. The more detail oriented the producer is, the higher the quality of the final outcome. Naturally, higher control over production factors will increase the production costs. Thus, wine producers are faced with the trade-off between cost and quality in an attempt to control natural processes. Although modern technologies have helped to increase control processes, and thus quality inspections, they have also contributed to mass production. This mass production has flooded the market with low-quality, low cost wines.

In order to control of the quality of wine and to assure consumers of its origins, the certificate designation of "protected designation of origin" (PDO or DOC in Portuguese) was created (Robinson, 2006). This system of certification depends on the:

- Geographical delimitation of the area
- Type of soil
- The authorized and recommend varieties of grape berries
- Agricultural practices
- Wine production methods
- Alcoholic percentage requirements
- Productivity per hectare
- Oenological practices
- Physical and chemical properties

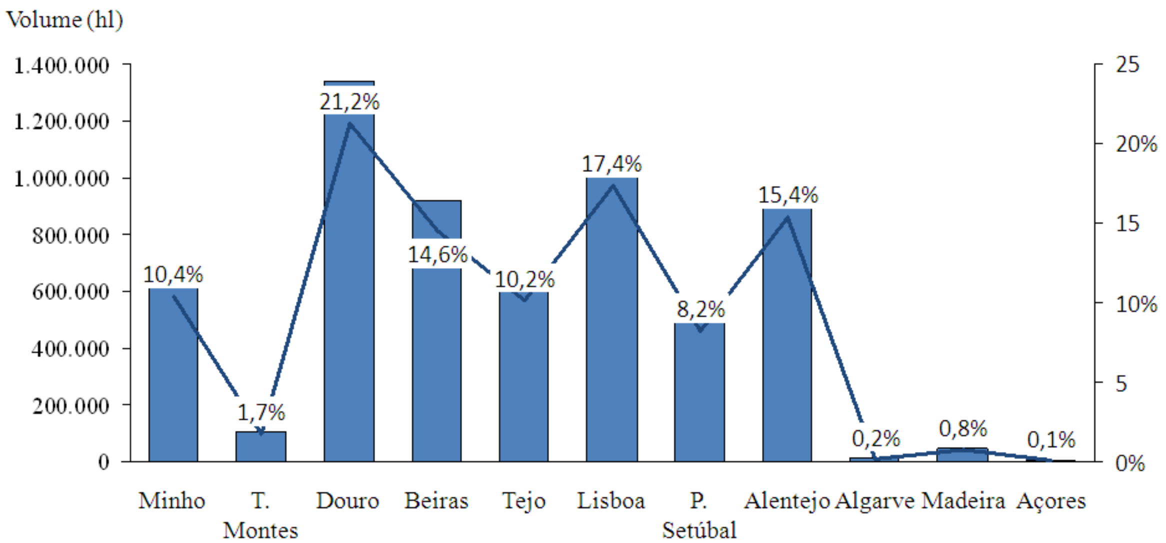
Currently Portugal has 29 PDO regions, spread all over the country. It is the final combination of all the previous factors that will determine the wine's quality and therefore how it will be presented to the market. It is completely different to sell a wine from the Douro/Porto PDO or the Setubal PDO. The main challenge presented to companies, which are usually based in a single region, is to make the most of the surround environment and use the right methods at their disposal to produce their wine at the highest quality. Instead of facing the environment as an inevitable condition, successful companies must use it as a competitive advantage as such resource is available only to a certain amount of companies, since it is an immobile resource (Barney, 1991).

MARKET ANALYSIS

Agriculture, forestry and fishing represented 2% of the total national production, according to the national statistic institute (INE, 1995-2010). Of those, approximately 13% of the generated value is from wine production (IVV, 2009). However, each wine region has contributed in a different way, as Figure 15 reveals.

The weight of each region in the total wine production in Portugal has been relatively stable throughout the years, except for Alentejo which has more than double is production since 2000 (IVV statistics). The Douro region produces approximately 134M litters or 21% of the total wine produced in Portugal and is the largest t contributor. The region with the lowest production levels is Azores, with approximately 497k litters or 0,1% of the total production.

Production per Wine Region

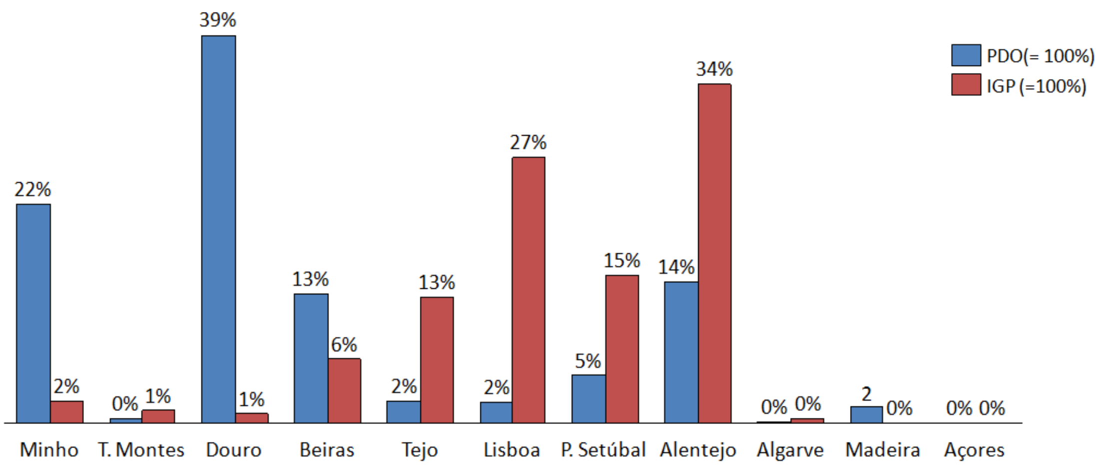


Source: IVV Statistics

Figure 15 – Production per Wine Region, 2012

Within this overall wine production, it is possible to separate between wine production that is certified as "Protected Designation of Origin" (PDO) and wines certified as "Protected Geographical Indication" (PGI). This last one certifies agricultural products and other related food goods that are closely related to a geographical area and in which "at least one of the stages of production, processing or preparation takes place in the area", according to the European Union definition (Geographical indications and traditional specialities, EU website).

Certified production per Wine Region



Source: IVV Statistics

Figure 16 – Contribution for each certified label, per wine region, 2012

Overall Portugal produces approximately 279M litters of PDO certified wine and 147M litter of PGI certified wine. Analysing by the type of certification, being PDO the hardest to obtain and thus the most valued, there are great disparities between regions. The Douro region, for instance, produces 39% of all of the PDO wine in Portugal while only contributing with 1% to the PGI wine. Minho is in a similar position as Douro. As the wine production moves to the south there is an increase contribution in PGI wine and a decrease in PDO. Lisbon, for example, is in a completely opposite situation than Douro or Minho. This region contributes with 27% of the overall PGI wine but only with 2% of the overall PDO. Alentejo is in a similar position as Lisbon, although not as in an extreme situation, with a contribution of 34% to PGI wine and 14% of PDO wine. Nonetheless, it is worth mention that this region has been increasing nearly every year its production, but more importantly its certified production. Since 2000 Alentejo has increased its PDO production approximately 70% and its PGI by 158% (from 23M to 39M litters and 19M to 50M, respectively), according to the IVV statistics.

This analysis shows within Portugal there are several contexts that vary from region to region. On one hand, the Douro region, despite only having one PDO designation – PDO Porto – is by far the largest producer of PDO certified wine. This is due to historical reasons, since this was the first PDO region in world, established in 1756. Lisbon, on the other hand, has 9 PDO designations but only produces 2% of the overall PDO wine in Portugal. Naturally, the consumers' perception affects this reality. Since the Douro region has such an historical weight it's more valued than the other regions. However, it is possible to conclude that there is an opportunity for a region such as Lisbon to increase its PDO wine production. This would require, naturally, a collective effort within the Lisbon producers to increase the region's perceived wine value.

Consumer

Portugal has a consumption of approximately 42 litters of wine per capita. However, this value has been decreasing over the last years, from around 65 litters per capita in 1990 and 45 litters per capita in 2005, according to the Instituto da Vinha e do Vinho (IVV, 2013).

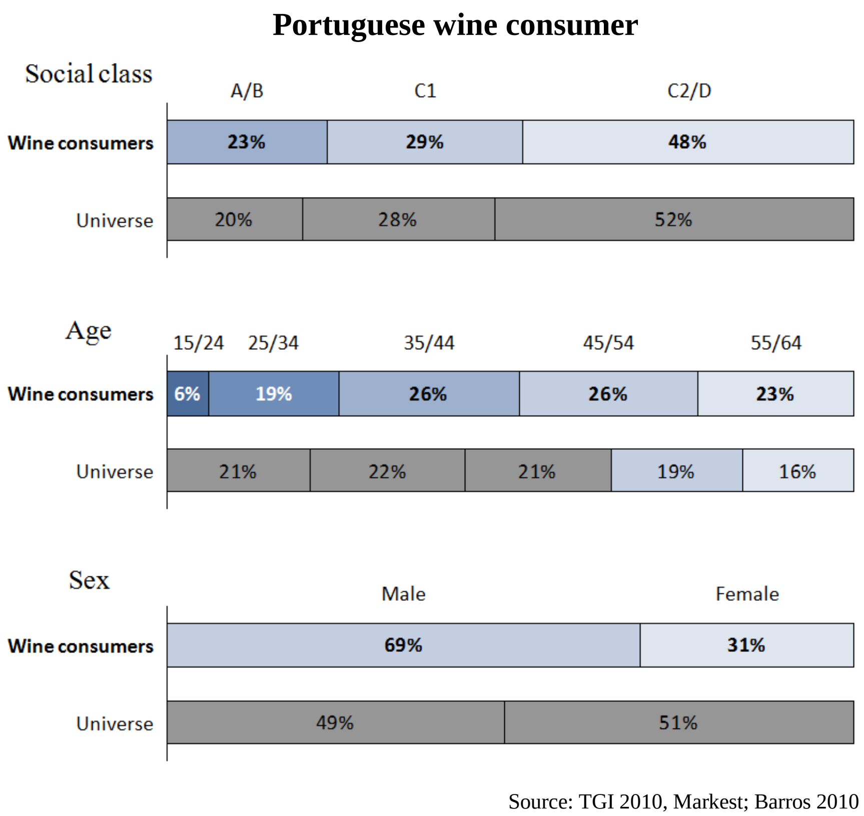


Figure 17 – Wine Portuguese consumer

The average wine consumer is not the typical Portuguese consumer. While there are more women in Portugal (51% versus 49% of men, Census 2011) there are more male wine consumers than female consumers. Regarding age, the average wine consumer is typically older, with a higher representation of 45 to 64 year old bracket. The 35 to 44 year old group is also more represented in the wine consuming population than in the Portuguese universe. Regarding income, while only 20% of the Portuguese population is in the A and B group, according the Markest segmentation, where A is the higher income class and D the lowest, there are 23% of wine consumers in this high-income groups, in detriment of the lower classes (C2 and D), comparing a 52% value in the Portuguese population but only 48% in the wine consuming population. Thus, the average wine consumer is richer, older and typically male when compared to the average Portuguese consumer.

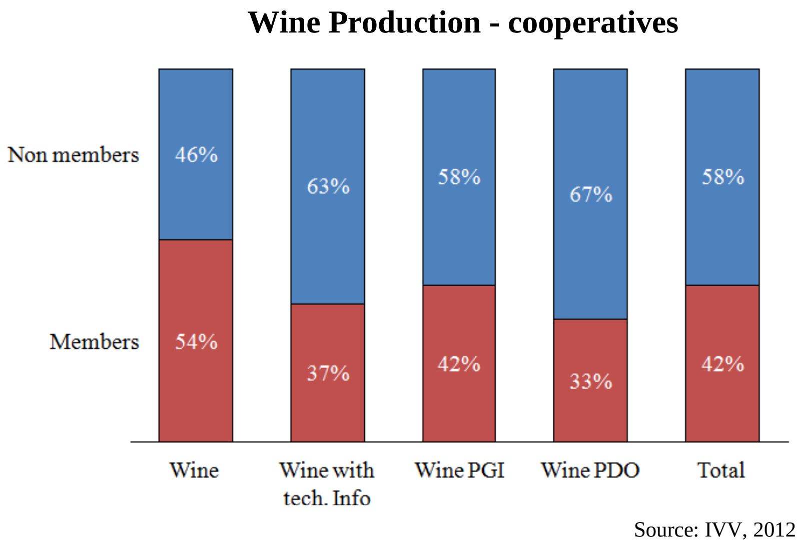


Figure 18 – Wine Production, divided between wine cooperatives member and non-members, 2012

Wine cooperatives are associations of, typically, small wine producers. With these wine cooperatives the small wine producers are able to split costs and it’s easier for them to invest as a whole in technical machinery and expertise. The wine producers are responsible for delivering wine to the cooperative which is then responsible for processing the product until it is ready for selling and then sell it (J. Robinson, 2006). Bigger and more advanced technological companies are usually out of cooperatives. Figure 18 illustrates how the Portuguese market is divided in terms of wine production. General wine, with no technical information or PGI/PDO certification, is mainly produced by wine cooperatives (54% vs. 46%). Once the technical requirements are higher to obtain then the wine cooperative starts to lose ground to the non-cooperative members. Regarding wine that has technical information, but with no PGI or PDO certification, non-members produce 63% vs. 37% of members' wine. The same happens with PGI and PDO wine. However, as the PDO certification is the hardest to obtain, it is where non-member production is more predominant with 67% vs. 33%. This is a clear indication that non-member production is, usually, a more sophisticated production. It's important to highlight that, since big wine producers are non-members of cooperative, the predominant wine production in Portugal is PDO certified. In fact, the Portuguese market is one of extremes. While there is more PDO wine, the second most produced is general wine ("wine" in figure 18). PDO production accounts for nearly 273M litters while general wine accounts for 195M litters. Wine with technical information but no certification has a small representation with only 2M litters. PGI certified wine accounts for 143M litters. Thus, it's possible to conclude the Portuguese wine market is a sophisticated market, where big wine producers dominate the high-value wine production and small, non-sophisticated wine cooperative producers have a higher representation in the low-value market.

THE COMPANY

As previously mentioned, for confidentiality purposes the name of the company will not be disclose. As such the characterization may, at time, be somewhat generic.

The company which is the subject of this thesis is a small, according to the EU definition, company located in the Lisbon area. Its run by the 2nd generation of descendents of the company's founder and should, in the medium term, pass on to the 3rd generation. It is therefore a family-owned business who is more concerned with the long term success of the business than with short term dividend payouts. In the last years the company was able to benefit from European funds that help it to modernize its factory and production system, along with its headquarters. The company sells the wine it produces, with no association with a wine cooperative, although sometimes it requires to buy grapes from micro nearby producers to meet demand peeks or to add a certain wanted characteristics to one of its crops. Although the company has a deep understanding of the wine market, the author believes there is the need for a clear vision to guide the company's performance and strategic decisions, which is a key factor since people tend to focus on their daily operations overlooking the bigger picture. Also the majority of the wine sold is of the low added value kind. With the resources the company as there a great potential to succeed even further and meet the customer's needs while at the same time providing a valuable service, shifting the focus from a wine producer to a company that sells the wine drinking experience.

With the current economic crisis, like other companies, exports have been an important way for the company to do business and minimize the impacts of the decrease in demand for wine. Government and public institutes have been trying to stimulate exportations either trough fiscal incentives, credit lines or reduced bureaucracy (Competitividade, Emprego e Investimento, 2012). The more the company exports, the less depended it is from internal demand and the more countries it exports to, the more diversified the risk is. By exporting to different countries and different continents, companies can take advantage of high-growth economies while minimizing their exposure to recessive economies, such as Portugal in the last years.

Nearly 30% of all of the company's production goes to exportation. This represents roughly €470k, with 85% of production going to non EU-countries. Main importers of the company's wine are:

- **EUA** – In partnership with ViniPortugal, a Portuguese wine-trade association whose mission is to promote Portuguese wine, spirit drinks and vinegar in international markets, the company has been present in wine tasting events alongside other Portuguese companies. Importers, distributors, HORECA channels and final consumers are present at such events. The company also has a commercial assistant *in situ* that prospects the market and provides assistance to existing clients. Good reviews in wine-specialized magazines have helped to gain new customers. Some importers have exclusivity rights, although the company believes it has a diversified-enough portfolio so importers don't have conflicting interests with the same state. Products to this market are of the medium-high and high category products, representing 15% of exports.
- **China** – The most time consuming market due to bureaucracy issues. The exporting process is very complex with several legal compliances needing to be fulfilled. Conditions vary from region to region. While in Hong Kong and Macau there is no import-taxes, other regions have an average of 40% of tax over the product value. Through networking, there have been Chinese delegations visits to the company's headquarters. Periodically the company sends partners to China to provide assistance to existing customers. In terms of quality, all kinds of wine are shipped representing 15% of exports.
- **Mozambique –** A local intermediary makes the bridge with wine importers and develops promotion events *in situ*, mainly in commercial spaces, in direct contact with the final consumers. Acknowledging the fact this is not a fully matured market, most products are of the low and medium quality variety. The country represents 15% of the volume.
- **Canada –** The company is present in only one state, in the British Columbia. As this is a monopoly system, controlled by each State (except the free market system in Alberta and the mix public-private market in British Columbia), the products need to be approved state by state. In the British Columbia, the market is highly regulated with the state attributing licenses to sell alcoholic beverages to a very few privately-owned retail stores. Also, the State has its own alcoholic selling retail stores. The opportunity to export to Canada derived from a single importer that showed interest after experiencing the product in the USA. The company is present in the few privately-

owned retail stores with plans to be in the public retail stores. The medium quality variety is shipped to Canada, representing 10% of exports.

- **Holland, Germany and Denmark** – These markets are similar in many aspects, in terms of exports for the company. Contacts were initiated through international fairs or by visits of potential clients to the cellar. Exports are of the medium and premium quality with each country representing 5% of total exports, thus 15% aggregated.
- **Cape Verde, São Tomé and Principe and Congo –** Contacts with these countries are all done through an intermediary that establishes himself the connection with local importers. Like Mozambique, exports to these countries are of the low and medium quality. In total it represents 30% of exports.

The company has plans to extend to England, through a supermarket chain distributor, Brazil, Sweden and Finland through contacts with local importers. Sweden and Finland have the particularity of being a State-monopolized market (Systembolaget in Sweden and Alko in Finland).

Product

The company produces wine, and in smaller quantities “aguardente” (spirit or liquor, although there is no exact translation to English). Within the wine category it has 2 kinds of wine:

- **Table wine** - low/medium quality wines. It has 8 different brands with all of them having the white wine or the red wine variety. Alcoholic strength varies from 12º to 12,5º and bottles have 1l or 0,75l capacity. 2 of the brands are also available in the Bag in Box (BIB) packagings. BIB containers are inexpensive, more easily stored and less likely to break compared to bottles and have ecological advantages (Yam, 2009). Scientific research on wine conservation (R. Ghidossi, 2012) indicate that for red wine BIB storage is similar to glass bottles while in white wine conservation it has worst results. Nonetheless, in the consumers mind, BIB is still associated with cheap, low quality wine (Official Board Markets, 2012).
- **Regional wines** – medium/premium wines. It has 9 brands, all of them red wine, with 2 brands also having wine white. Out of the 9, only 1 is PDO (DOC in Portuguese). This is in fact the only PDO wine the company has. With this certificate the wine is assured an immediate reliability in terms of meeting certain quality standards thus being valued more highly by customers. However the awards go to the other brands. One brand has two national awards and another one has one national award and an

international one, won in Vienna. Awards matter as they become selling points, since it reduces the buyer's risk in acquiring wines since by whatever quality standards the contests in question had, the award one was the best. This immediately differentiates the wine from its competitors and awards the winning wine with free, specialized and targeted advertising.

Financial Analysis

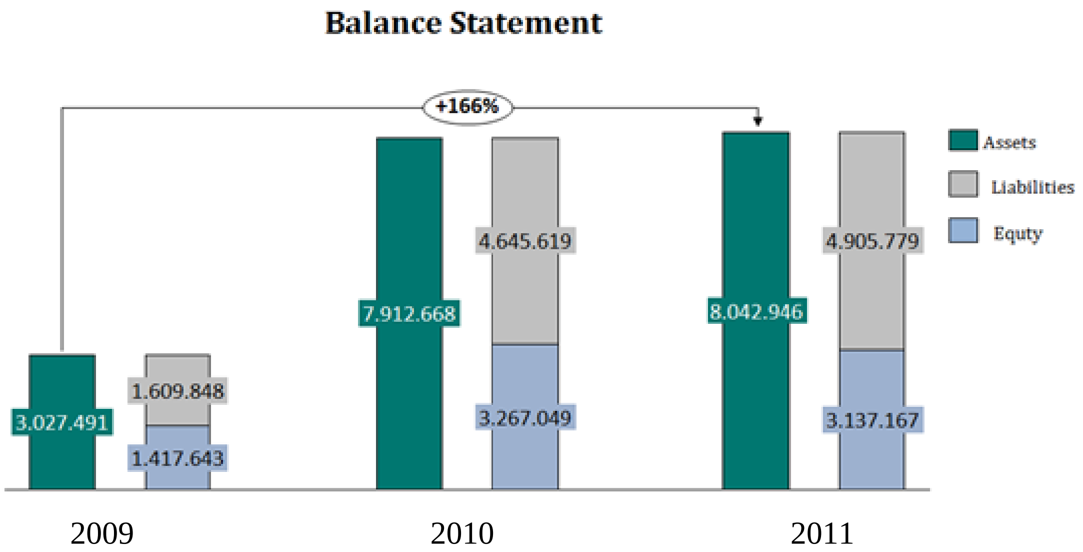


Figure 19 – Balance Statement, from 2009 until 2011

The company has seen a vast increase in its assets. In just 3 years, the company's size, as measured by its asset's accounting value, has grown by 166%. The investment in a new headquarters/factory was responsible for such a growth. Tangible assets grew from €1.1 million to €6 million in 3 years. With no substantial increase in revenues, this investment has had a strong negative influence in both Gross ROA and Net ROA, causing it to decrease by 76% and 87% respectively. Decreases in Asset Turnover, or the ability the company has to generate revenue from its assets, show exactly this with a 66% decrease from 2009 to 2011, from a 2009 value of 57% to 20% in 2011. With an increase in assets, investors expect companies to increase their revenues. A new factory may mean more products being produced and thus sold, for instance. However, so far, that has not been the case, as revenues have not increased. The intrinsic characteristics of the wine industry are also responsible for such a decrease in profitability. This industry is characterized for testing investors' long term commitment as wine is a slow and quality-ageing product. The wine being currently produced in the new facilities will only reach the market in 2/3 years. If by then the situation remains the same, either the investment was a poor judgement call or some other factor was responsible for the continuously low profitability. Also, the current economic crisis has had a negative impact in the company's ability to generate profit, as Portuguese's purchasing power has decreased.

There are two events that need to explain with more detail. The company had to record a loss on its retained earnings of €140k as a result of bad debt on behalf of its clients. Although some bad debt is always expected this amount accounts for nearly 9% of total sales volume. Unquestionably the current economic crisis is a cause for such event and this example shows the effects of such crisis in companies, particularly in "business-to-business" markets. The second event is an increase of nearly €1,2M in the "Other equity instruments" rubric due to a subsidy received by the "Instituto de Financiamento de Agriculturas e Pescas" to help finance for the new headquarters.

Profitability Ratios

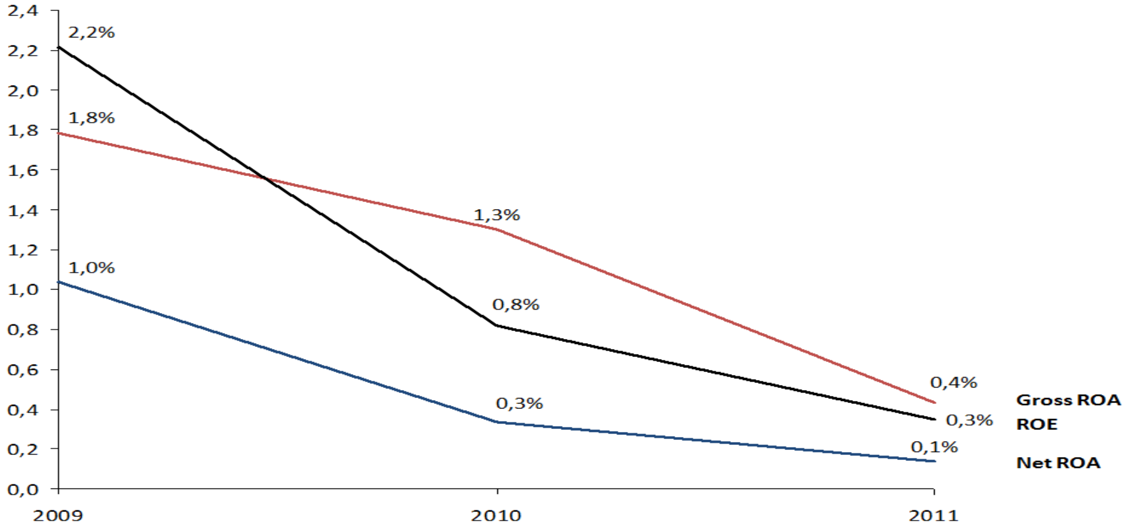


Figure 20 –Profitability ratios, Gross ROA, ROE and Net ROA, from 2009 until 2011

Consequently, the investments made in 2010 have also not yet yielded in net income, something that takes its toll in the company's ROE. With ROE yielding a mere 0,3% in 2011 the company's shareholders gain nearly 0% on its investments. As the company is not seeking new investors, this low ROE may not have short-term effects. Nonetheless, this indicator may predict future disinvestments by current investors, in an attempt to invest their money more efficiently. Only the family linkage of the shareholders, as this is a family-owned company, may protect the company from sell-outs. However, banks tend to analyse these profitability ratios like ROA and ROE, among other, as a measure of financial slack and future growth.

With a 0,3% value of ROE and 0,1% of Net ROA, the company is clearly not very efficient in generating profit. According to Yahoo Finance, in a 58-company analysis of the Beverages - Wineries & Distillers industry, the average industry ROE is 24.1% (Yahoo, Industry Browser), clearly above the company's ROE.

Financial strength is also important as companies need to have some muscle to withstand slow economic times, as the one currently unfolding in Portugal. Investors look for solid companies as they are more capable to "weather the storm" with banks practicing lower interests on their loans to these companies, since the risk of defaulting on their credits is lower. In terms of financial capacity the company is completely within industry standards, with a 129% long-term debt to equity ratio in 2011 (industry standard: 129,16%) and an equity ratio (equity/assets) of 39%. Although those ratios have been decreasing throughout these 3 years (91% long-term debt to equity ratio and a 47% equity ratio in 2009), they remain at completely acceptable levels.

However, profitability and financial strength are not the only key factors. Liquidity is also important as it analyzes the company's ability to convert assets in to cash quickly, thus its ability to pay its short term debt. The company's Current ratio and Acid Test determine exactly this. These Ratios analyze the relationship between current assets and current liabilities. The difference between them is the Acid test is a stricter test, as it does not include inventories as current assets. In times of financial distress inventories may not be as liquid as in normal economic times, so less likely to generate cash. Although both ratios consider Account Payable, the same effect may be present, as it may be difficult to get clients to pay their debts. A higher than 1 result indicates the company is able to pay its short-term debts. In the wine industry there is, however, a special consideration that needs to be taken in account. As wine ages in the company's cellars to obtain a richer taste and improved quality, it is not uncommon for wine companies to have higher inventories then what would be considered normal in other industries. The Acid test eliminates this effect by not considering Inventories.

	2009	**2010**	**2011**
Current Ratio	6,0	5,3	2,4
Acid Test	2,3	3,4	1,3

Clearly the company is able to meet its short-term obligations, as in every year it has had >1 results. However, the 2009 and 2010 company's Acid Test of 2.3 and 3.4, respectively, deserve a closer analysis. These values indicate that in these years the company was inefficiently using its current assets, which ultimately represent cash that was either tied up (accounts receivable, for instance) or not being put to the best use (accumulation of cash and cash equivalents). As “cash and cash equivalents” has never represented more than 6,8% of currents assets - 6,8% (2011); 1,6% (2010) and 3,1% (2009) - it’s clear the problem isn´t cash not being put to the best use. Either the company is too quick in paying its suppliers compared to the time it takes to convert inventories into cash, something usual in the wine industry, or it could have taken greater advantage of short-term loans to invest in whatever opportunity. In fact, even if the short-term loans were twice as high for each year, the company would still have had a >1 Acid Test value in any given year. The company should resort more to this type of loan as short term debt is easier to negotiate since it does not need collaterals, is it also less expensive than long term debt and can be used to free up cash for business opportunities that would otherwise be foregone (Deal Flow – Debt Financing).

In terms of efficiency in their operations the company is also quite inefficient.

	2009	**2010**	**2011**	2009 -2011
Gross Margin	32%	40%	39%	22%
Net Profit Margin	1,8%	1,5%	0,7%	-62%

As expected in a wine company, raw materials have consumed a quite substantial part of revenues, nearly 65% of every euro-revenue. Nonetheless, the Gross Margin has improved by 22% since 2009 meaning one of two options, or both:

- The company has been more efficient in its production, spending fewer raw materials to produce wine. This effect would not impact revenues but would decrease the cost of goods sold
- The company has been able to sell more high-margin products. This could have increase costs (assuming premium raw materials are more expensive) but would have had a significant positive impact in revenues. Thus, for the same Euro spent in goods sold, there would have been more Euros per each good sold in revenues.

As revenues have not increased, and even decreased by 9% since 2009, the first option – more efficient production – is the most likely to be happening. This is consistent with the investment being made in new facilities that allow to efficiency gains. Profit margin however has sharply decreased by 62%, to a mere 0,7% of revenues. The company’s operation and financial costs weigh heavily on its revenues, making it very inefficient in generating net income. Increases in supplies and external services (+29%) and payroll expenditures (+14%) were the main responsible for such a decrease in net income. Nonetheless, even with the higher Net Profit Margin of 1.8% (2009) it is still a very low result. Yahoo's industry analysis - Beverages - Wineries & Distillers industry – benchmarks Net Profit Margin at 17%.

A Free Cash Flow analysis allows investors to determine if the company's operations are able to generate cash to invest in new business opportunities or distribute it to investors through dividends.

Free Cash Flow Analysis

	2009	2010	2011
EBIT	€ 53.949	€ 103.077	€ 53.949
NOPLAT	€ 50.387	€ 74.369	€ 36.620
Depreciations and Amortizations	€ 95.059	€ 55.925	€ 61.082
Net WC variation*		€ 1.641.674	-€ 1.215.385
CAPEX**		€ 3.035.771	€ 260.160
Free Cash Flow	**€ 145.446**	**-€ 4.547.150**	**€ 1.052.927**

* As there is no data for 2008, Net WC is assumed to be the same in 2008 as 2009, thus with 0 variation

** Calculated by the difference in Tangible Assets from last years' value

t = effective tax rate

Although there is a substantial negative value in 2010, the company is able to generate positive cash flows in 2009 and 2011. The negative 2010 value was expected, since there was a substantial investment in CAPEX, +3 million euros, in new facilities. In 2011 the company was able to reduce substantially the Net WC which allowed for a strong positive Free Cash Flow of +1 million Euros. This effect is a consequence of the previously seen more balanced values for the Current Ratio and Acid Test in 2011. With a more efficient use of Current Assets and Current Liabilities (Current Ratio and Acid Test closer to 1) the company was able to free up more money in 2011.

It's also pertinent to evaluate the company through a treasury equilibrium perspective. While Free Cash Flow analysis determines if the company was able to free up cash, after the investments it made, the Treasury equilibrium analysis evaluates whether the company's capital short term structure is optimal regarding its operations' cash requirements. Short term capital structure is evaluated through Net Working Capital. Operations cash requirements are determined by the Working Capital Requirements. In a perfect world companies would have just enough net current assets (deducted from current liabilities) to meet their short term cash operations. This would result a 0 value in Treasury Equilibrium. A significant positive value indicates the company has too much current assets, and consequently it is not used them in the most efficient manner. A negative Treasury Equilibrium value indicates the company will need to resort to some sort of funding, either Equity or Debt. To determine if the value is too positive or too negative (inefficient use or funding requirements) the Treasury Equilibrium can be compared to the amount of revenues.

	2009	2010	2011
Net working Capital	€ 1.583.552	€ 2.798.937	€ 1.157.263
Working Capital Requirements	€ 1.678.444	€ 1.605.023	€ 1.001.760
Treasury Equilibrium	-€ 94.892	€ 1.193.914	€ 155.503
T.E. as a % of revenues	-5%	68%	10%

In 2009, as inventories represented 60% of current assets, the company despite having a current asset value 600% higher than its current liabilities (as seen by the Current ratio value of 6) had negative treasury equilibrium. Inventories are assets that have not been converted into cash and are thus a capital requirement. As they represented a significant part of the capital structure, this capital requirement reflected on the negative treasury equilibrium. Had the company been able to convert its inventories into cash, its Working Capital Requirements would have been lower, resulting in a more positive Treasury Equilibrium. In 2010 the opposite happened. The company had a €1.2 million increase in the “Other receivables” rubric, thus with no effect in Working capital Requirements, resulting in a Treasury Equilibrium surplus representing 68% of revenues. This €1.2 million increase was the result of equipment sale, related to the new facilities process. Thus, the company had €1.2 million tied up, with it was not able to use to invest in business opportunities. Only in 2011 does the company achieves a good Treasury Equilibrium, with a surplus that represented 10% of revenues, a value considered within normal parameters acting like a safety net.

The company is a typical Portuguese family owned medium enterprise. It has solid financial position, which is important in today’s economic crisis. This financial strength is key to negotiate long-term debt contracts as it lowers credit default risk. In terms of operations, it’s very inefficient in generating Net Income, although it has been improving its Gross Profit values, through a decrease in the cost of goods sold. Only in 2011 has the capital structure been more efficiently used to generate cash, as seen by the Current Ratio, Acid Test and Free

Cash Flow analysis. There is a greater margin to take advantage of short-term loans that could help obtain short-term business opportunities. However, this should not be the company's primary funding process. The company needs to take advantage of the new facilities to generate more revenue and in a more efficient manner. The supplies and external services and payroll rubric should be closely monitored since they have had a strong negative impact in profit generation.

Setting the new paradigm: experience-based differentiation

As identified by the Marketing Future Cast Lab (2102), “Experience Based Differentiation” is a marketing trend that enables companies to create a brand experience in every point of contact with the customer, building stronger brand identities with a lasting commitment with the consumer based on emotional aspects. Also, Norman (2001) talks about the importance of the “Experiencification” concept) when making a transition from product to offering, in accordance to the Service-Dominant Logic. Normann (2001) describes it as the connection between product/service with customer. He also believes in the importance of rebundling into new patterns what has been unbundled, creating more dense value offers while trying to fill the client’s needs. Several authors talked about this “experience marketing” concept in an attempt to define and provide insights about it. However, according to Tynan (Tynan, 2009) “the gulf between academics and practitioners on this topic [experience marketing] is now as wide as ever with bestselling titles on experience marketing written by and for practitioners, which are rich in examples and step-by-step guides to managerial success yet pay scant attention to the contributions of academics in this area”. Also, she claims “Service-Dominant logic is employed to bridge the divide between theory and practice in this respect”. All these arguments support the importance of Service-Dominant Logic as a way to help companies gain what is considered by Barney (Barney, 1991) as a sustained competitive advantage, such as the connection between brand and consumer, or “brand experience”. This thesis aims to analyze all this concepts applied to a small-medium enterprise in the wine industry in Portugal.

Thus, it’s imperative to identify the consumer’s experience related to wine as a whole. By separating the different phases, unbundling the process as Normman (Normann, 2001) refers, it’s possible to identify areas to either enhance the experience or to create new ones, including the re-bundling of existing ones. The following figure identifies a typical and extensive wine consumption scenario. Different scenarios may not follow all of the identified phases, but follow no less.

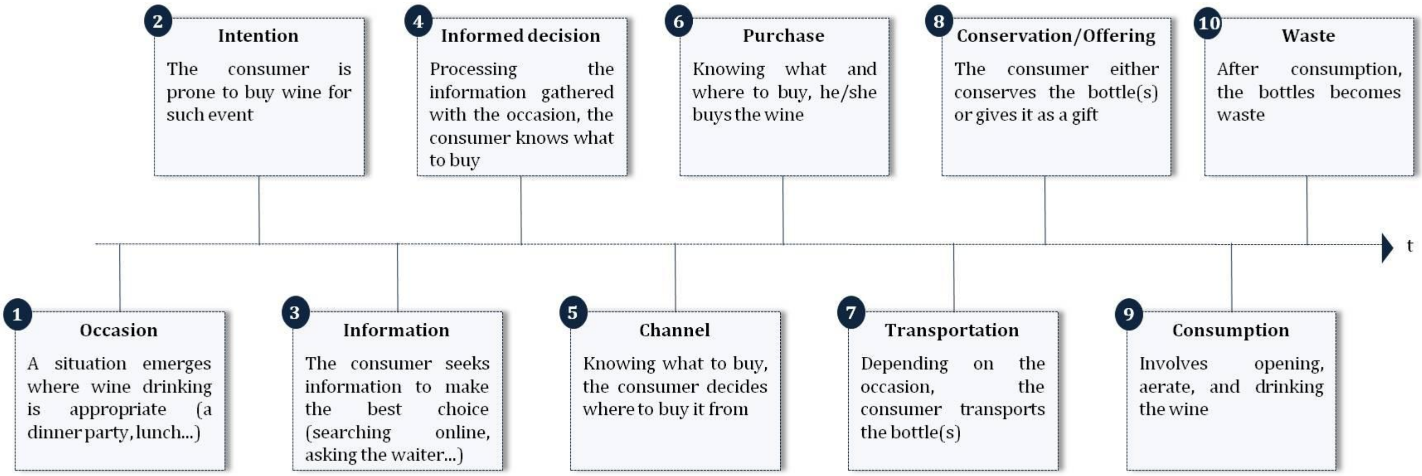


Figure 21 – The consumer wine experience

Phase	Opportunities	Points of Contact
Occasion	Celebration of special occasions (e.g. Birthdays, Christmas,…) with friends and family	Event-oriented communication, reminding people of special dates Event-targeted promotions (birthdays, anniversaries, family celebrations…)
Intention	The consumer acknowledges that buying wine is appropriate for such an event	Communication emphasizing the portfolio of the company, reminding the consumer it has a wide variety of wines
Information	The consumer looks for accessible, easy to understand, relevant and useful information	Multi-platform information – website, apps, bottle label Simple and direct information
Informed decision	Assuring the consumer he has made the right choice	Peer recommendations Sharing other consumers experiences Promote the awards won, reassuring the consumer of his/her choice
Channel	Adapting the consumer's needs to available channels	Wide variety of channels to buy from – online, phone, restaurants and other commercial areas
Purchase	The willingness of the customer to buy wine is in itself the biggest opportunity	Simple and quick buying process Provide several payment options for online and telephone purchases
Transportation	Provide the customer with a comfortable way to transport the wine	Have easy to transport packages Capture value with extra features (e.g. express delivery)

Conservation /Offering	Few consumers know the appropriate way to truly conserve wine There is an opportunity to make the costumer look good when offering the wine	Provide the customer with proper conservation information and tools – Conservation Have a good external presentation and a fashionable gift package - Offering Provide extra-services such as label personalization or gift card offering - Offering
Consumption	The consumer values the taste of the wine and requires certain consumption objects (glass, corkscrews, wine cooler, wine collar…)	Provide several merchandised good to improve the consumption experience
Waste	The consumer is left with waste that needs disposal	Collect the consumers empty bottles, using them to recycling purposes and giving him/her a benefit on the next purchase

Table 3 –Proposed experience-based differentiation

It's the sum of the different phases that creates the whole customer experience. For the company to be able to create a connection with the customer, it must be there for him/her in every step, creating value along the whole journey, but without imposing. Thus, for every phase of the experience identified, there is something the consumer perceives as value added. For each phase, there are different needs and opportunities. In the following table, the "Opportunities" column is the combination of needs and possible opportunities. The "Points of Contact" is how the company can enhance the experience, creating a connection with the consumer.

Occasion

People enjoy celebrating special occasions. Whether it's someone birthday, wedding anniversaries or getting a good grade, Portuguese people like to commemorate these special events. As such, wine and food is always associated with celebrations. The company can thus target these special events with communication and discounts.

In terms of communication, the company can, via social media and website, remind people to celebrate those national special occasions (Christmas, Easter and all kinds of holidays) with a bottle of wine. In 2012, the company did a **single post** on Facebook on the 20th of November 2012, one month before Christmas. That was all of the promotion the company did online targeting Christmas. Certainly it is nowhere near the optimal level of promotion to take advantage of such an event to stimulate consumption. Like Christmas, there are different holidays throughout the year the company can take advantage of.

Another kind of events is those concerning individuals' lives. If someone has moved into a new house, if his/her birthday is in a week's time or if someone has a new job, that person is going to want to celebrate it with his/her friends and family. Facebook, for instance, allows companies to target these 3 special events with ads. In March 10, 2013 there were 176,960 people in Portugal that fall within one of those 3 categories (birthday within 1 week, moved into a new house or has a new job) over 18 years on Facebook. This represents a 176 960 potential market[4] that can be targeted with advertising, while the company chooses whatever budget it deems fit to spend (more budget means more ads and exposure naturally). These ads should serve as bait to get people curious about the product and wanting to find out more, by visiting the website or facebook page. However, there must be something else to stimulate the purchase. Considering such situations don't occur more than once a year, especially regarding birthdays, the company should start giving **discounts on people's birthdays**, with a margin of one week before or after the purchasing day (people usually prepare birthday parties with a week in advance or delay, depending on what day of the week the birthday is). This can be easily done by having the customer submit its ID copy online or show it upon delivery. These discounts can be more creative such as showing a student's grade report to celebrate its graduation or wedding certificate to celebrate a wedding anniversary.

Intention and Information

Different wines suit different occasions. A summer holiday may require a cool white wine or a winter holiday a red wine. Red wine is also appropriate for meat courses while white wine is typically served with fish. A business event requires a more premium wine while a quiet evening in-house may be suitable for a medium quality wine. Thus, in order to stimulate the consumer to choose the company, it's necessary to communicate the wide variety of wine the company has. The key message is that no matter the event in question, the company has the right offer for it.

Thus, integrating with the following phase, where the consumer seeks information, there is the opportunity to gap the bridge between commercial information (discount, prices) and a more technical one.

[4] Calculated via Facebook Ads simulation on 2013-03-10

The company's website should have a set of questions to help people choose the right wine. The following structure is proposed to help consumers choose the best wine.

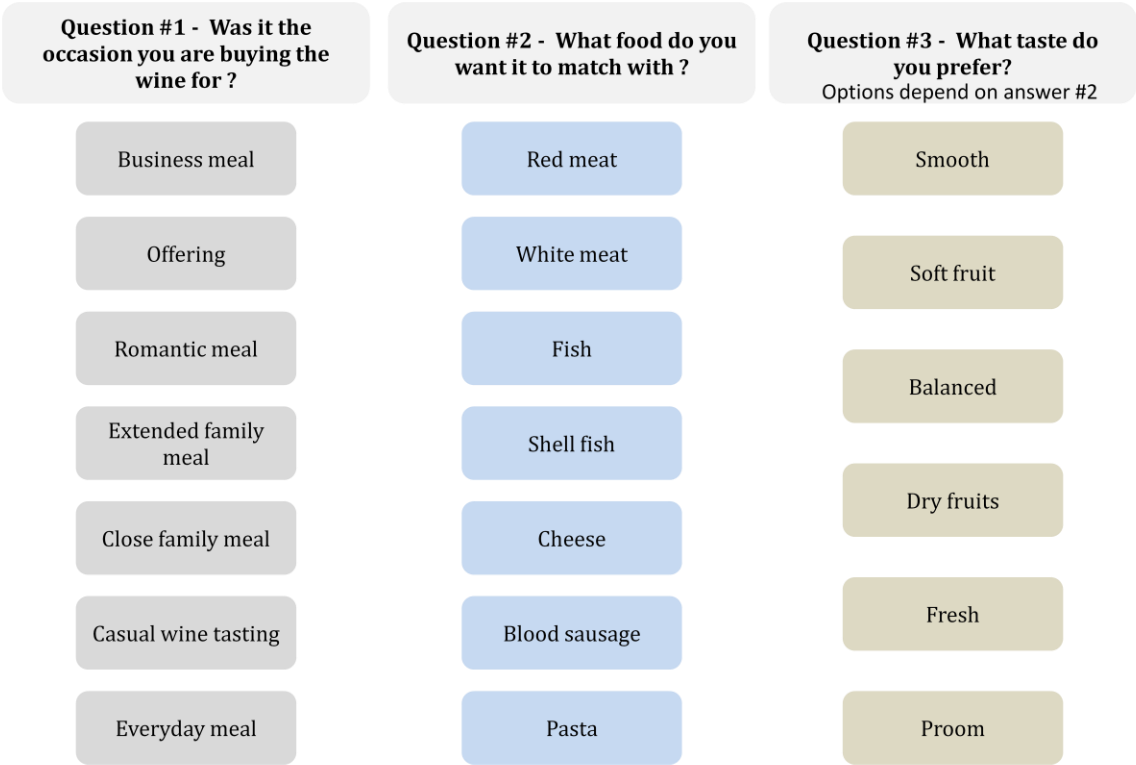


Figure 22 – Decision-making questionnaire for consumers

A combination between the 3 answers allows the company to target the best wine to advise the customer upon its purchase.

The first question determines if the recommended wine is from the premium, medium or low quality variety. The low quality is still a very good wine but it's not honest to recommend the consumer to buy the most expensive wine for an everyday meal. Naturally, the options available on question #3 are heavily depended on answer #2. Red meat can be accompanied with a soft fruit or a dry fruit flavoured wine, but not with a fresh tasting one. So, by asking 3 simple questions, conditioning the available answers when appropriate, in a quick and straight-to-the-point questionnaire the company is able to advise the consumer in a non-intrusive way on the most suitable wine for the occasion. The consumer will acknowledge the help provided and feel more confident in its future purchase, knowing he has chosen the right wine. This creates goodwill and confidence towards the company.

Informed Decision

So far the consumer has received the advices from the company. Although it's a professional opinion, it's clear for every consumer that it is not an impartial advice since the ultimate objective is to sell wine. There's no point in trying to hide this fact which every consumer knows. Communicating the awards won by the company in national and international competitions is of great importance. This helps consumers to know not only the company strongly believes that its wine portfolio is of great quality, and based on the impartial opinion of national and international experts acting as judges in wine competitions. But alongside with these professionals' opinions, consumers also value peer recommendation. This is where comments and feedback from other consumers and recommendations from its fellow peers will ultimately convince the consumer of its choice. Thanks to social media this can be done in a fairly easy manner. Engaging in tryvertising campaigns, asking for people's feedback about the products is the way to do so. Tryvertising, a combination of "try" and "advertising", is defined as getting the consumer to experience the product in a casual and non-intrusive way (Marketing FutureCast Labs 2012). This can be done offering wine bottles to selected consumers who are willing to try them and then give honest feedback about it. The company needs to be sure about its product's quality to move forward this experience, since negative feedback cannot be hidden online, although positive one should be highlighted. Ensuring product's quality and a carefully assessment of consumers to ask feedback from is key. The content of the feedback can take all shape and sizes. Videos, texts, pictures posted in social media websites or directly in the company's website will accomplish the goal of provide new customer with feedback from existing ones. An online rating system for each wine variety is also a tool to use. Much like in the hotel industry, consumers go online to rate positive or negative experiences, typically in a 1-5 or 1-10 rating scale. By doing so with its wine portfolio, directly in its website, the company would accomplish two goals: the one discussed, providing new customers with existing customers opinions and getting a market response of its brand variety. Poorly judged wines could be candidates to a discontinuation process, giving the company a quick and easy market feedback tool.

Channel

Different consumers enjoy buying using different channels. Some consumers are willing to waste more time to see the bottle itself and to get a real feel of the product. Others want to be able to buy anywhere anytime, through an online channel. According to INE (INE,2012), in

2012, 13, 3% of the Portuguese population did online shopping. The same study concludes that regarding education levels, 36,6% of people with a college degree did shopping online in 2012. Other consumers may want to buy wine in the comfort of its home, but not online which some view as unsafe or lacking the digital literacy to doing so. Telephone orders are a solution for such consumers. The key idea is to provide a multitude of channels to buy from, without having to cope with significant investments. The main channels are:

- Online orders – Online store provides a 24/7 availability not offered by any other channel and a worldwide reach. E-commerce solutions are widely available in the Internet. The bigcommerce.com or shopify.com websites allows a company to set up an online store for nearly €25 a month, with variable conditions including integration with delivery companies for calculating instantly shipping rates and security certificates. The 3 key success factors behind an online store are: 1) to have a diverse offer to choose from, 2) to provide the customer with a user friendly experience, 3) to have a secure and operational platform. The payment can be automatically done in the website or upon delivery (a practice already used for orders placed via other channels). For a company with more than 1 million euros in revenues who sells to final consumers and has a wide variety of wines, an online store is a logical extension for its digital presence and distribution strategy. Also, through tools like Google Analytics, it’s possible to gather a multitude of information such as most viewed products, the time consumers spent on each product, their location accessing the website and many other data that can be analyzed by the company to generate valuable business intelligence. There’s also the possibility to create targeted online marketing campaigns, integrating it with the actions described previously. New customers need to be attracted through security measures and other consumers’ feedback while existing customers use the online shop to buy conveniently the products they already know. Cross-selling and promoting other wine varieties are key factors to incentivize purchases. Currently, the company doesn’t have an online store.
- Phone orders – Phone orders, although not available 24/7, allow consumers to order anywhere. The company already accepts orders via telephone, but in an indirect way. There is no information in the bottle label regarding which number to call to place an order. In the website there phone numbers to contact the company but no explicit one saying “orders here”, which may induce the consumer in believing that there is no phone order availability. There must be explicit information in every communication

piece saying which number to call to place orders. Telephone orders also provide a good alternative for consumers who are not digital literates, meaning consumers who are not able to effectively use digital technologies or for those that still wish to talk to a real person to place an order.

- Restaurants, trade fairs and other commercial areas – this has been the company's ongoing strategy, to focus in physical channels, where consumers can actually feel, touch and analyze the product. These are the typical channels in the wine industry. The downside is that in these places there are also a variety of competitors for the consumer to choose from. A wide reach of stores selling the company's wine products are essential so the consumer has several options to buy the product from. Marketing actions to get the consumers attention is what drives sales. However, these actions cannot be inconsequent actions and need to part of a broader strategy. The consumer needs to pay attention to the product, buy it and then continue to be a customer, using the same channel or the other proposed channels. Some examples of attention-getting strategies:
    - Appeal to the consumer's senses stimuli – creating bottles that appeal to consumers touch and sight (taste and smell is already present in the wine itself; hearing is something that can be intrusive), through the wine labels or the bottle itself, is something that can differentiate the company's products regarding other competitors. Examples of such stimulation can be visually appealing wine labels or bottles/labels with interesting textures (see examples below). These must follow the company's brand identity and with each wine's variety and personality.



Purchase and Transportation

If the customer's experience has been properly structured up until now, then purchasing the bottle of wine will seem the most logical step for the consumer. However, if not properly designed, the purchasing experience can actually drive customers away. Especially in online purchases it is very important to provide the customer with several payment methods such as credit cards, pay pal or pay upon delivery (for customers who do not trust in online payment systems). Whether it's in online channels or in physical ones, there is always an opportunity for the company to capture more value in the transportation of the products. Customers may be willing to pay an extra-fee for more express deliveries when buying online or an extra fee to have the products delivered to him/her at home, when buying in a physical channel. Whatever the channel used the purchase, it must be as simple as possible, while assuring that the costumer is feeling safe in the purchase.

Conservation/Offering

Wine has specific conservation methods. Usually companies tend to put this information in the wine label. The company also presents this information in its wine labels. However, an avid wine consumer has the need to storage the wine and for that it requires certain accessories, which may vary according to the specifications or aesthetic purposes. To fulfil this need, and since it's not the company's core business to sell these accessories, the company needs to establish strategic partnerships. By choosing the right partner, whose core business is to sell such products, and recommending them to its customers the company is able to once more fulfil a customer's need, creating value for it and thus strengthening its value proposition to the consumer. There is also the possibility to create bundles so that is it's cheaper, and more convenient, for the consumer to buy the bundle than the products separately. This could also be something done exclusively over the online store to foster it awareness and incentivize consumers to use the online channel. For such recommendation, depending on the partnership, the company may gain a fee. Eurocave, a French company specialized in wine cabinets and other wine conservation items, is an example of such a possible partner. Another strategy is to order directly from a white label manufacturer and place the company's brand in it. The contacts the company has in china could serve such purpose. However, this strategy requires an investment upfront that, while it's not perishable, may take some time selling to customers, especially in the early phases which would mean having cash tied up on such products, which are not the company's core business.

Since wine is sometimes purchased to be offered to other people, there is also an opportunity to charge special fees for sensorial impressive packages, appealing to both the customer and the person receiving the gift. These special packages can be simpler or more complex. Naturally, the more complex ones are more expensive but they fulfil the customer's need to impress the person receiving the gift. By making the value offer denser, more fulfilling of the customers' needs, the company is able to capture additional value. Such offers should be heavily communicated to coincide with special seasons of the year where people tend to offer gifts (e.g. Christmas) or targeted to special events in people's lives, as discussed previously in the "Occasion" phase. This is an example of the importance to integrate the different phases identified in order for the company to be able to view the costumer's experience as a whole, integrating the different phases.

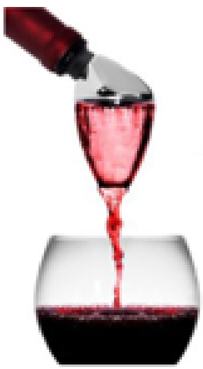
Consumption

Drinking wine can sometimes resemble a ceremonial event. Although not everybody follows all the steps, there is a process in drinking wine. Therefore, the customer also has specific needs for this phase, which the company can fulfil. In this phase, the action plan is to provide merchandising products, so the consumer is reminded of the brand, even when consuming competitor brands. Also, the products serve a useful purpose in themselves. Consciously or not, the consumer associates the company with the merchandised products, so quality (not easily breakable) and fashionable/design goods must be the chosen products. Depending on the product, the company can either use them to have a higher value proposition to the consumer by giving them away in marketing campaigns or by selling them to gain some of the money invested in the products. Since it's not the company's core business to produce such goods, and it would not be efficient in doing so, it must seek suppliers that can meet the company's demands and standards of quality. Alternatively the company may establish partnerships with companies whose core business is to sell such products. The North

American company IWA (International Wine Accessories) specializes in such products. Partnerships such as this would guarantee the quality of the products provided, assuming such company is willing to stamp the company's name in their products, but this would come at higher costs, since the company would need to pay a higher price to IWA than it would pay a white label provider.

The first step is to remove the foil and open the bottle. In order to do that a customer requires a **wine bottle opener**, usually with a foil remover included.

The next step is to decant the wine. This serves two purposes. One is to let the wine to came in contact with oxygen so it can breathe, improving its aroma and taste. The other is due to the fact that older wines tend to have a small amount of solid matter, as a consequence of its long resting time, so there's the need to separate the amount of liquid containing sediment from the rest of the wine, a process called decanting the wine. A **decanter** serves both purposes but it's possible to buy an **aerator** that while it doesn't separates the solid matter, lets the wine breathe.



After the wine has breathed and is solid-matter-free, it is ready to be served. In order to serve, the consumer requires a **glass** to pour the wine and, although this is optional, he/she may also require a **wine pourer** to keep drops from spilling out. The glass is the object the consumer holds for the longest time in this consumption experience, so the marketing impact (the company logo/lettering) needs to be subtle, otherwise it may be perceived as an intrusive and too-much campaign. Nonetheless, because the consumer holds the glass while talking to its friends for a reasonable amount of time, there's an opportunity to stimulate consumer interaction. The proposed way is via a **QR code embedded in the glass**. A QR code is a matrix barcode invented in Japan by a Toyota subsidiary "with the primary aim of being a symbol that is easily interpreted by scanner equipment" (QR Code website). Using a smartphone, a person is able to scan the QR code with the device's camera, which may contain information such as the company's website (re-directing the person to it) or a pre-made post to share on social media platforms such as facebook or twitter. According to *Scan.com*, a specialized QR code company, QR codes may contain information to allow people to (Scan.me website):

- "**Business Scan Page** - a mobile friendly menu which enables your customers to easily interact with and share your business "E.g. provide more information regarding the company, its website, its social media platforms, contact information, typical business card information…
- "**Social Media Actions** - create social experiences through QR codes: Scan to Like on Facebook, Scan to Follow on Twitter, Scan to Check In on FourSquare, and more" E.g. a quick and easy way to gain fans, likes, followers online. It helps to promote the company online
- "**Website** - take your users to any URL. It is best practice to make sure the page is optimized for mobile devices" E.g. provide a direct link to the company homepage or directly to its online shop (described earlier, in the "Channel" phase)
- "**Simple Text** - Display a note or message" E.g. a simple text thanking the customer for choosing the company's products or just "Enjoy your wine" kind of messages

Even with the QR code, the company should still have fashionable wine glasses and pourers and if it's able to combine both the QR code with fashionable products the more impact it will cause.



The elements presented so far as the most essential. However, the company can have a whole array of accessory products to keep surprising the customers. Coasters, glass identifiers (for social situations), vacuum pumps to preserve open bottle longer, wine coolers for wines best served at low temperatures, wine cooling drops are such examples.



A phased launch of the proposed products is the recommended strategy. On one hand it's doesn't involved so much investment in buying the products in a short period of time. On the other hand, by releasing products over a longer period of time, it provides the company with useful regular content to connect with consumers. The key factor in choosing future merchandised products is to provide useful objects the consumers will actually use, thus fulfilling a real need while at the same time associating the act of drinking wine to the company's brand.

Waste

The final step in the consumer experience is the waste he/she is left with, the empty wine bottles. Normally the customer would throw these empty bottles away, thus finishing the experience. If that was the case, the connection between company and consumer would be over. The whole experience would start again almost from starch, loosing consumers along the way. So it's important to keep the connection with the consumer, looping the experience but leveraging on the previous one. If the company is able to take advantage of the previous experience it will need to spent less efforts retaining the customer and thus more able to capture new while keeping existing customers. The empty wine bottles are what enable the company to leverage on the experience, making it so the consumers continue in a looping cycle. Instead of regarding it as trash, the company can turn them in marketing objects. A sort of pyramid scheme can be devised to reward higher ranking customers:

- Up to 10 empty bottles (and more than 5 bottles) – a 1% discount on each empty bottle, on the next order
- From 11 to 15 empty bottles – a 1% discount on each empty bottle, on the next order, plus an offer of a merchandising product (a low-cost one)
- From 16 to 25 empty bottles – a free bottle of wine of the costumer's choice, on the next order
- More than 25 bottles - an offer of a merchandising product (a more valuable one)

By placing the next order, the costumer would inform the company it had empty bottles ready for pick up and how many he/she had. Using the company's existing distribution force, the distributor would pick up the bottles, certifying the actual number of bottles and giving the customer the promised offer. The company could them use the empty bottles for recycling purposes.

Customer Experience as a whole

The purpose in analyzing step by step the consumer's experience is to identify possible points of contact between the company and customer, where the first can add value to the second. No single phase, done separately, is enough for the company to have a sufficiently dense value proposition. In other words, if the company doesn't adopt a transversal approach to the customer's experience and instead only implements a few, disconnected proposed action plans it will not be able to gain and retain customers. Having an online store doesn't attract customers by itself nor does having a QR code in wine glasses. However, offering a complete integrated value propositioning to the customers will, as the company will be able to fulfil all of the customer's needs, even the ones the customer may not be aware of. Ultimately, the flow of the whole experience must seem as natural to the customer, as one phase links to the other, even if he/she isn't aware of it. This value proposition, based on the consumer's experience, will enable a relationship between company and customer, thus resulting in a sustained competitive advantage (Barney, 1991). This change in the company's mindset shifts its focus from selling wines bottles to provide a pleasant experience in consuming wine. In fact selling bottles of wine is merely a single phase of the all experience. As such, focusing solely on that phase dooms the company to a myopic view of the overall paradigm and cripples it to a narrow and insufficient strategic view of the market. The final objective is not to gain customers but to gain supporters, people who will actively recommend the company to its peers. The transformation from customers to supporters is the best outcome a company may hope for, especially in today's competitive market.

Business Case

A solid and sustainable value proposition is the key element to company's success. Without it, a consumer is not attracted to the company's products/services and, therefore, it will not generate any revenue for the company, leading to its failure. Consequently, a successful value proposition can only be considered as such if it leads to a company's financial success. Without financial success a company cannot expect to continue to operate in the long term.

Thus, the next logical step after the proposed value proposition is to elaborate a business plan in order to assess the cost of the proposed actions and the expected benefits driven from such actions. Estimates are based on benchmarks, information provided by the company, data gathered via professionals working on the question at hand (particularly website's, app's and advertising costs) or due to strategic decisions. The analysis follows an incremental approach, meaning costs will only be considered as such if they represent an added cash outflow that would otherwise not be taken if it wasn't for the strategic action proposed. The costs are assumed to start at Year 1 as expenses are of an operating nature and, as such, take place in the same time period as revenues. The analysis is a 3-year analysis as after such period cash-flow is expected to stabilize. From that period on, new strategic actions would have to define that would affect the following forecast. Taxes will not be considered because the profit generated from the proposed strategic actions can be invested by the company in other activities.

Estimated costs are as follows,

	Source	Benchmark	Year 1	Year 2	Year 3	Notes
Event-oriented communication		CPC: 0,10€ (experts)	500 €	1.000 €	2.000 €	
Other institutional communication		CPC: 0,10€ (experts)	500 €	1.000 €	2.000 €	
Develop app			755 €	180 €	468 €	Includes developer licensing (upgrade in 3rd year)
Develop website		tinyurl.com/bhydctk	2.500 €	1.200 €	3.600 €	OPEX + development
Develop bottle label design	Company		700 €	-	800 €	The company has easy access to designer work
Simple and direct information						No cost can be inputted to such activity
Peer recommendations						Consumer's activities
Sharing other consumers experiences						Via marketing tools; free
Promote the awards won						Via marketing tools; free
Development of online shop		www.shopify.com/pricing	1040 €	540 €	1.632 €	Fees + web developer assistance
Simple and quick buying process						No cost can be inputted to such activity
Provide several payment options						Included in ecommerce tools
Have easy to transport packages						Included in overhead costs
Extra features (e.g. express delivery)						Extra-features inputted to the customer
Provide the customer with proper conservation information and tools						Conservation tools paid by the customer
Gift offering related services						Paid by customer

Provide several merchandised goods	Strategic decision		300 €	300 €	700 €	Working Capital
Collect the consumers empty bottles for marketing purposes						Included in overhead costs (for online purchases; other channels already require meeting the customer in person)
Total			**6.295 €**	**4.220 €**	**11.200 €**	

Table 4 – Estimated Costs of the strategic actions

The key assumptions are as follows,

	Year 1	**Year 2**	**Year 3**
ARPU (without VAT)	7,32 €	8,94 €	9,76 €
% of consumers/visitors*	10%	15%	18%
Increase in visitors yoy		100%	100%
Overhead (% of sales)**	15%		
r (cost of capital)	6,19%		
Cost of goods sold (% of sales)	60%		
g	0,5%		

*visitors are people who visit at least one of the company's online touchpoints

** Overhead costs represent costs dependent of sales or otherwise too dependent of external factors

Table 5 – Key assumptions

The Average Revenue Per User (ARPU) is an indicator to identify how much a customer pays, on average, in each purchase. The values were given based on the company's experience. ARPU grows each year as the company is able to capture more value, taking advantage from relationships established in the previous years and as a result of increased exposure of communication strategies. This communication strategies aim to increase the number of visitors in the company's online touchpoints. As first-time online satisfied consumers keep visiting the site to make more purchases, the ratio between consumers and visitors tends to increase each year. With the increase in the budget spent each year to attract online leads, it is also expected that on a year to year basis the number of visitors increases. In fact, it could be argued that visitors could increase more rapidly than the money spent on communication due to word-of-mouth and network effects. However, one can also argue the more massive the communication is, the less effective it becomes, and as such visitors wouldn't increase as much as the communication budget. Thus, to counterbalance to the two effects, it is assumed the number of visitors increases as much as the budget, keeping the Cost per Click (how much the company pays to online advertisers such as Google or Facebook for each click derived from online advertising) at €0,10. Overhead costs account for fees that online payment companies tend to charge, typically between 2% to 5%, leaving a margin of approximately 13% to 10% of sales to account for extra-non-foreseeable costs, a sort of safety margin. The interest rate, "r", is calculated according to the Capital Asset Pricing Model (CAPM). The CAPM states that the cost of capital is . The risk-free rate is given by triple A rating bonds. Through the ECB website, seen on the 1st of July, it is possible to assess the risk-free rate is 0,5%. The beta unlevered , used instead of the levered one because the analysis is independent on the way on how it will be financed, for the alcoholic beverage industry according to the Damodaran website is 0,5. The market risk premium ( ), taken also from the Damodaran website, is 6%. The same source indicates the Country Risk Premium (CRP) for Portugal is 4,88%. Thus, computing all of the previous elements results in an interest rate of 6,19%. This is the interest rate at which to discount future cash-flows.

The cost of goods sold is reflected as a percentage of revenues and is taken from the company's income statement. The growth indicator "g" will be used to assess the terminal value. The 0,5% value was chosen to indicate a perpetual almost neutral growth, in order to keep a conservative estimate.

With the previous costs and key assumption, the financial results of the proposed actions are:

	Year 1	**Year 2**	**Year 3**
Visitors[5] (online)	10.000	20.000	40.000
Consumers	1.000	3.000	8.000
ARPU	8,13 €	8,94 €	10,16 €

Revenues	8.130€	26.829€	78.049€
Cost of goods sold	4.878€	16.098€	46.829€
Overhead	1.220€	4.024€	11.707€
Costs (strategic decisions)	6.295€	4.220€	11.200€

[5] Taylor's, one of the most known Porto wine sellers in Portugal, has approximately 720 000 online visitors annually, based on Alexa.com, a web information company

Total Costs	12.393€	24.342€	69.737€
Profit	-4.262€	2.487€	8.312€
Contribution to profit (2011 basis)	-39%	23%	76%

Table 6 – **Financial results of the proposed actions**

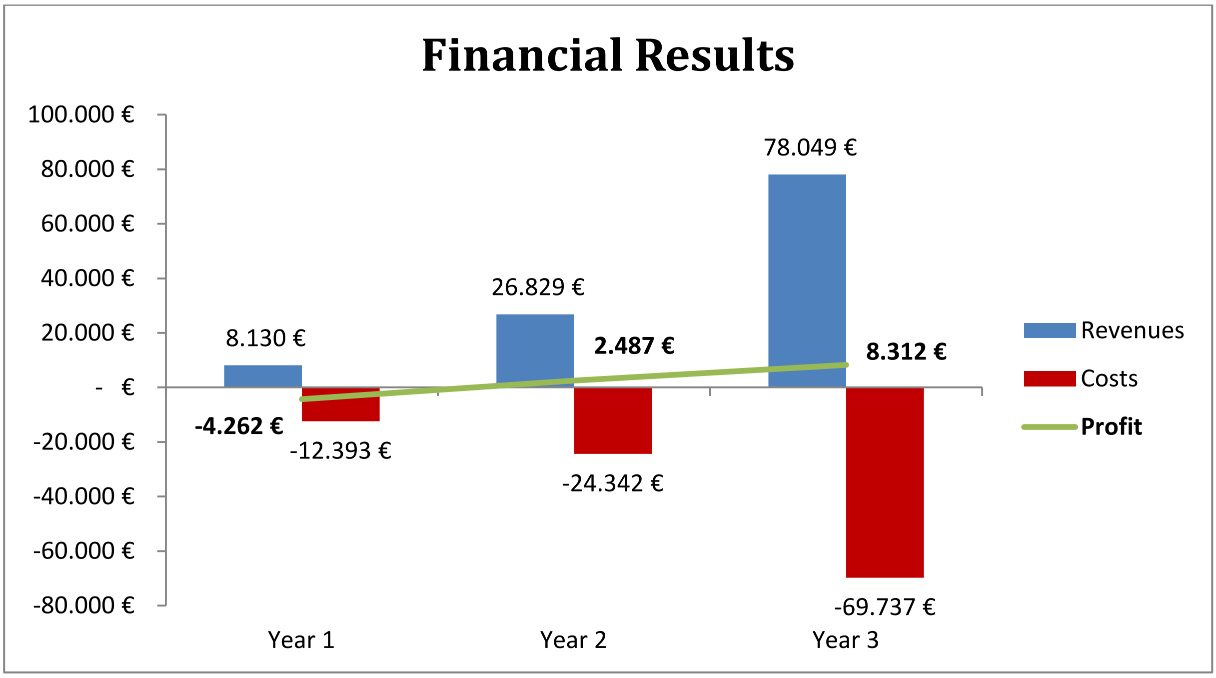


Figure 23 – **Financial Results – Revenues; Costs and Profit**

Considering the given rate of discount of 6,19% it is possible to calculate the Net Present Value (NPV) of the project. A positive NPV would indicate the proposed actions are profitable and should therefore be undertaken. Also, by calculating the Internal Rate of Return (IRR) it's possible to assess the rate at which the NPV would be 0. Although there is no alternative project to compare different IRR's and to choose from, the fact the IRR is much higher the cost of capital (72% vs. 6,19%) is an indicator that the project highly profitable. Also, it is reasonable to calculate the terminal value since the proposed actions continue to capitalize in the future. The 0.5% grow rate is used as an indicative value for future nearly stabilization of cash flow growth. As the Terminal Value is highly sensitive to changes in the grow rate, a 0.5% value is a reasonable conservative estimation. Thus, the Terminal value is approximately €146k. This means that, theoretically, just by investing in this strategy, the company increases its value by approximately €151k (NPV + Terminal Value), when compared to a 2011 profit of €11k.

Net Present Value	**5.133 €**
Internal Rate of Return	**72%**
Terminal Value (g=0,5%; r= 10%)	**146.084 €**

Table 7 – **NPV, IRR and Terminal Value**

The previous results, NPV and Terminal Value, are highly dependent of a certain variable, which in fact there's is no 100% infallible way to calculate. The variable described is "r", or the cost of capital. The value of 6,19% is based on exogenous variables, that basically may change every day. Therefore it becomes relevant to analyze how changes in the interest rate affect the financial valuation of the proposed strategies.

However, as long has the "true value" of the interest rate is below the IRR, the project continues to have a positive NPV. It is therefore necessary to compute a sensitivity analysis to evaluate how the NPV and Terminal Value would vary depending on variations of "r".

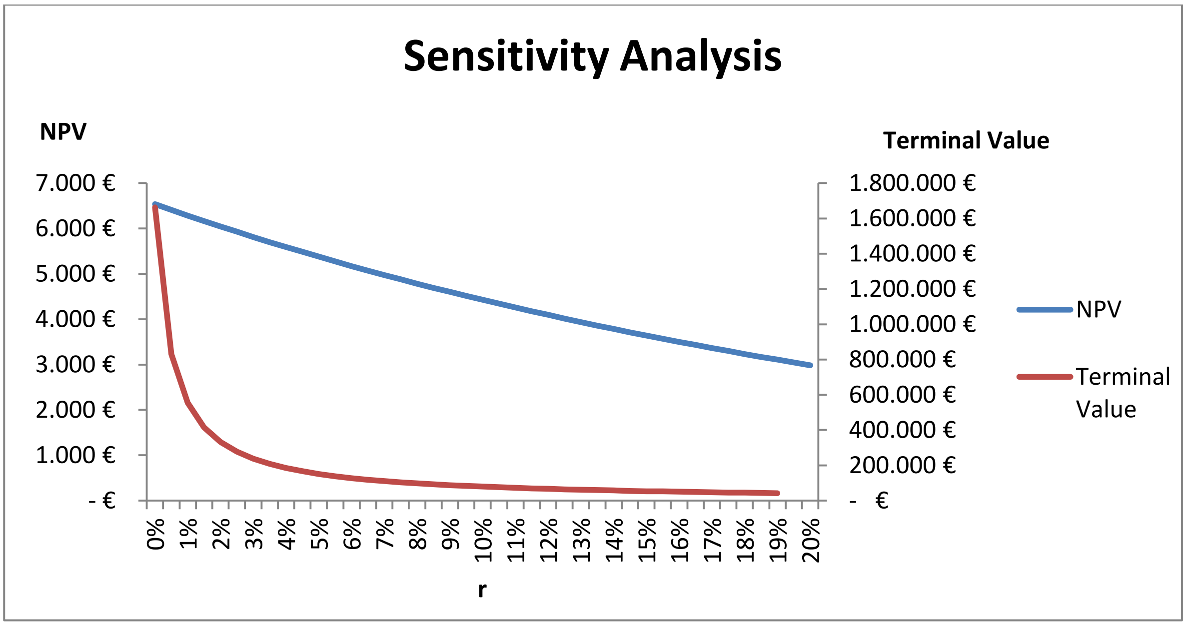


Figure 24 – **Sensitivity analysis**

Key figures:

r	NPV	Terminal Value
1%	6.286 €	1.662.439 €
5%	5.377 €	184.715 €
10%	4.426 €	87.497 €
15%	3.640 €	57.325 €
20%	2.986 €	42.627 €

Table 8 – **Key Figures – Interest rate, NPV and Terminal Value**

The sensitivity is particularly relevant in the terminal value calculations. A change of 1% to 5% in the “r” results in, approximately, a €1,5M variation. Nonetheless, even with a cost of capital as high as 20% the NPV would still be nearly 30% of 2011’s Net Income and the Terminal Value would be as high as €42k. The sensitivity analysis demonstrates that although the values may differ a considerable amount, the values remain positive and worthy of investment.

A financial analysis is always based on assumptions and, as such, it can never be infallibly accurate. However, the more solid the assumptions are, the more accurate the end result will be. To prevent misjudgement calls, sensitivity analyses help to determine what the risk level is. The outcome of the previous analysis is that financially speaking it makes sense to invest in the proposed actions. The success of such actions may differ depending on the accuracy of the assumptions but there is economical reasoning for the company to pursue such strategy. Also, some key metrics are extremely difficult, if not impossible, to quantify or calculate. For example, with the increased exposure, the company may gain a new business-to-business opportunity. An importer in some country may be in contact with the company’s products and choose to place a large order. Previous consumers may gain a new found appreciation for the company, which would in turn reinforce their loyalty in the company. The increased brand value could result in future business opportunities such as media coverage and awards. The increase in sales could help the company to improve its bargaining power with suppliers, forcing the costs down. The possibilities of indirect benefits are vast and even if not taken into account in the financial calculations due to their inherent unpredictable nature, should account for a small factor in the decision-making process. What this analysis has proven is that there is economical reasoning to invest in the proposed strategy. Certainly risk will always be a part of the equation but in this increasingly competitive world companies must strive to be ahead of their competitors, to gain sustainable competitive advantages and to deliver value to its stakeholders.

CONCLUSION

This thesis has as its starting point the analysis of the importance of sustainable competitive advantages for companies and how the service-dominant logic can be used by companies to reshape its strategic vision and, consequently, its value-added process. The increased value density of the company's offerings is a key element to gain the discussed sustainable competitive advantages. 3 concepts guide the business reshaping process: *Servicification*; *E-fication*; *Experiencification* (Normann, 2001).

The purpose of the thesis is to apply service-dominant concepts and frameworks to a traditional family-based Portuguese SME in the also traditional wine market, despite its limited resources. Thus, the subsequent analysis focused on analysing the Portuguese economical, social and environmental context.

The national market is truly a fertile one for wine companies to prosper, either by taking advantage of the Portuguese environment and producing great quality wine to sell overseas or by selling to its national intense wine consumption population, which ranks in 4^{th} in the world ranking in terms of wine consumption per capita (see figure 12). Naturally the downside is the intense competition and wide availability of cheap high quality wines in Portugal.

Following the external analysis, it was indispensable to perform an internal analysis of the company, focusing on how the company operates nowadays and what its financial resources are. The internal analysis showed that the company is not yet at its full potential and could be more efficient in the use of its resources.

This analysis has set to reshape the company's strategic vision from a wine selling company to a company that sells the experience of wine drinking, thus providing a comprehensive customer experience. In fact, selling the physical bottle of wine is merely a part in the overall experience. Therefore, consumers become an intrinsic part in the creation of value and, throughout their interactions with the company along the whole process are able to personalize their own experience to fit their needs. Thus, the company gains a sustainable, or long-term, competitive advantage in the market to face its competitors.

In order to be successful the strategic vision must, however, translate in financial success. A comprehensive analysis of the costs involved and expected outcomes was done in order to access the risk involved in the implementation of such strategy. These estimates carry, undoubtedly, an amount of uncertainty inherent to every financial analysis. To reduce the uncertainty of the estimates a sensitivity analysis based on variations of the implied interest rate was done, along with it's the impacts in the NPV and Terminal Value. The outcomes clearly indicate that even in scenarios where the interest rate is 3 times higher than the assumed one, the NPV still has a solid positive impact in the company.

This study faced several limitations. The most relevant one is related to the confidentiality issues that the company's top management has imposed and, as such, the company's name is never revealed nor any other information that could single it out. Naturally, this has had some impacts in terms of the volume and detail of information disclosed particularly in the internal analysis. Also, there was some information that either was not possible for the company to gather, due to a lack of records or inability to process data, or they had to perform a sort of ad-hoc analysis from their data to collect it, particularly information related to customer relationship management. These data limitations may have affected the quality and accuracy of the information used (e.g. the % of each international market in total revenue was gathered ad-hoc by a company's manager, since there was no structured report with that information). However, it is important to highlight that the company, whenever possible, has always supplied information and shown a great openness throughout the elaboration of this study.

Further research within the company context may follow two different but related vectors. On one hand it would provide an additional insight to deeply analyse how can the company measure and control the proposed actions' success or failure. The impact of such strategy can, and should, translate into material gains (increased sales for instance) but it can also have other non-tangible gains. Increased loyalty, brand-awareness or consumer's goodwill are examples of such non-tangible assets that the company may gain in the future as an impact of such strategy and that are worth analyzing on their own. On the other hand, the analysis of the next steps the company should follow after the implementation of the proposed strategy and how it can continue to create value for the customers and how to further integrate them in the value creation process would lead to a dynamic and virtuous feedback system of improving the strategic approach to the market.

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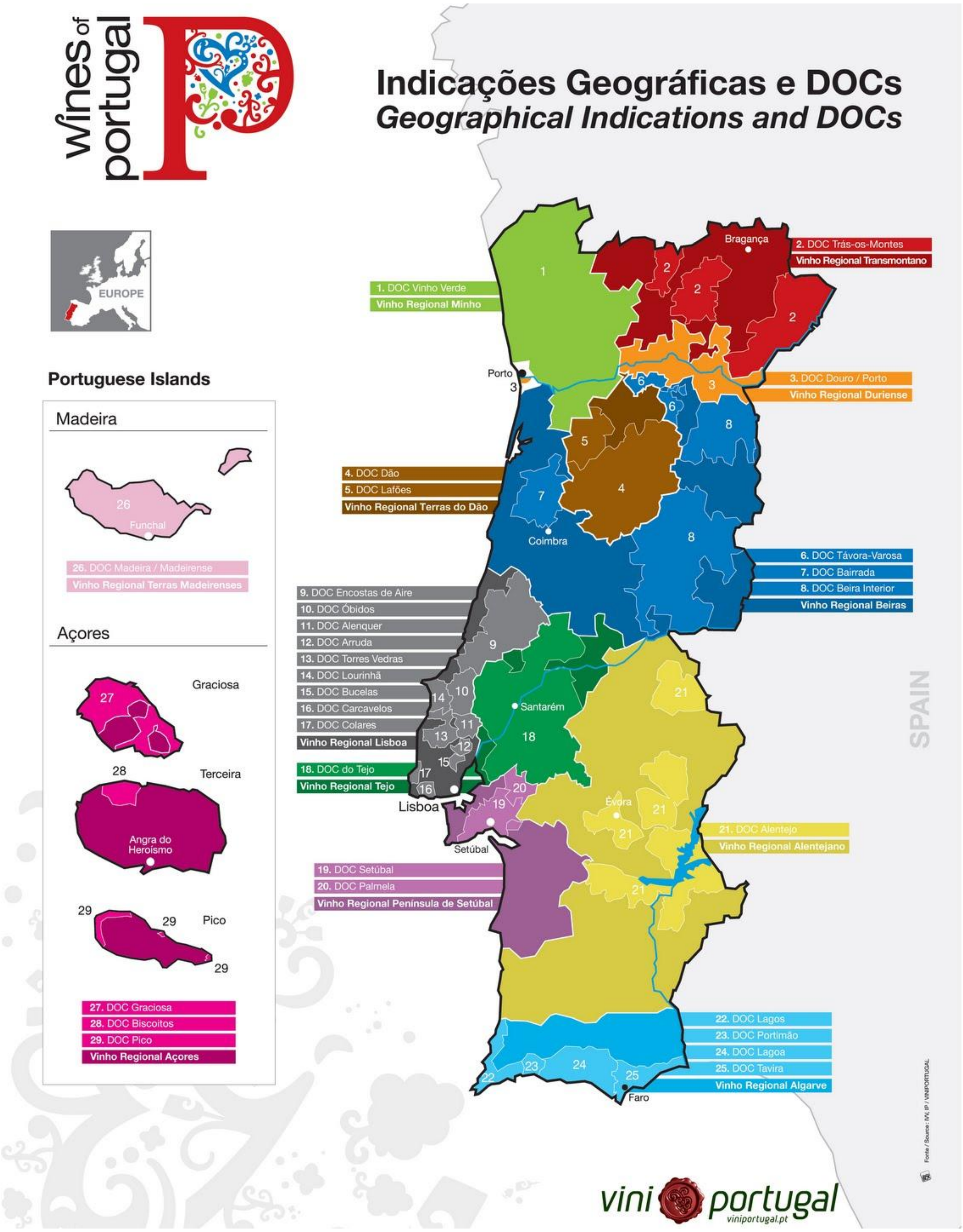
ANNEX



Annex 1 – Portuguese wine PDO variety and wine regions